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Nestor Healthcare Group plc

Annual Report and Accounts 2005



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Chairman's Statement

These results are the first full year figures to have been prepared in accordance with International Financial Reporting Standards (IFRS). Comparative figures have been adjusted accordingly.

Results summary under IFRS

	2005	2004
Turnover	£309.0m	£389.8m
Operating profit	£19.9m	£(41.9m)
Profit before tax	£14.2m	£(47.5m)
Earnings per share	11.7p	(57.1p)

The above operating profit figures include charges arising from IFRS changes of £948k (2004: £46k). These changes are analysed under "Impact of IFRS" below. Under IFRS 3, goodwill is no longer amortised on a regular basis but instead is subject to annual impairment reviews. Goodwill amortised in 2004 totalled £8.3m.

2004 results include exceptional costs relating to goodwill impairments and restructuring costs. The comparative figures for 2004 and the segmental analysis below, include these items as a deduction from operating profit.

	2005		2004	
	Turnover	Operating profit	Turnover	Operating profit
Healthcare Staffing	£113.1m	£4.3m	£155.1m	£1.7m
Social Care	£108.7m	£12.7m	£112.0m	£7.3m
Primary Care	£87.2m	£2.9m	£122.7m	£(50.9m)
	£309.0m	£19.9m	£389.8m	£(41.9m)

Business performance

For the purpose of comparison, business performance identifies the operating profit by sector, excluding those exceptional operating costs referred to above. The commentary by sector refers to business performance operating profits after excluding these items.

Excluding the effect of the change in accounting standards and adjusting for the profit impact of the 2004 exceptional costs, underlying profit before tax at £15.3m is marginally ahead of last year despite a reduction in turnover of £80m, or 20%.

Management's response to the changing and difficult market conditions in 2005 has been effective and is evidenced by the improved operating margin, which increased from 5.3% to 6.7%.

The reduction in turnover in Primary Care is as expected following the transfer of out-of-hours care to Primary Care Trusts (PCTs). This business is now solidly profitable and is providing a much improved quality of service. In Healthcare Staffing, we have seen a further decline in volumes to the NHS; however dependence on this activity has reduced significantly with the strengthening of business elsewhere in the Group. Social Care continues to perform well with a number of new contract wins in the second half of 2005 further enhancing the prospects of the business in 2006 and beyond.

Healthcare Staffing

	2005	2004
Turnover	£113.1m	£155.1m
Operating profit	£4.3m	£1.7m
Add back exceptional costs	nil	£5.7m
Business performance	£4.3m	£7.4m

Volume through the NHS, having stabilised for a period, has in recent months resumed its decline. The well publicised overspend in the NHS are having a significant impact on the demand for staff, both temporary and permanent, a situation exacerbated by an oversupply of certain professionals, for example junior hospital doctors and physiotherapists. Additionally, the new iterations of framework agreements are increasingly pressurising margins. Certain NHS contracts are now so marginally profitable that consideration will be given as to whether they are worth continuing with and contracting for in the future. In response the branch network has been rationalised and the focus for management is on growth away from the NHS in areas such as private hospitals, nursing and care homes, PCT prisons and occupational health. This change in focus will take time to achieve and in the meantime, where necessary, further cost base reductions will be implemented.

Social Care

	2005	2004
Turnover	£108.7m	£112.0m
Operating profit	£12.7m	£7.3m
Add back exceptional costs	nil	£4.4m
Business performance	£12.7m	£11.7m

The Social Care figures above for 2005 and the 2004 comparative now include business, largely domiciliary care, in Scotland, which

" Management's response to the changing and difficult market conditions in 2005 has been effective and is evidenced by the improved operating margin, which increased from 5.3% to 6.7%."

was previously reported under Healthcare Staffing. Overall Social Care margin has again improved to 11.7% from 10.4% last year. This margin improvement results from a number of factors. Firstly, 2005 sees the full year benefit from the reorganisation of Medico and Goldsborough, which commenced in 2004. In addition, our two private patient homecare businesses, Country Cousins and Patricia White's, both of which generate very good returns, had an excellent year, as did Carewatch where we continue to expand the franchise network.

The reduction in turnover is wholly due to our withdrawal from the Staffordshire contract in the early part of 2005 due to the onerous nature of the contract provisions. In our interim results statement we commented that, as Local Authority budgets were under pressure, pricing was becoming more competitive and this remains the case. However Nestor's reputation for quality, together with a fine tuned pricing strategy has led to a series of contract wins in the second half of 2005, with many more opportunities still outstanding. Most notably the Group secured the retention of the large Bedfordshire contract for a further five years. In addition a number of new contracts have been won, including Leeds, Barnsley, Worcester, the Wirral, Kensington and Chelsea, Leicestershire, Herefordshire and Lincolnshire. The annualised turnover of new and additional contracts recently won is approximately £6m. We also reported last year the loss of a major contract in Coventry; in fact very little volume has been lost as some of the new providers have failed to perform.

Primary Care

	2005	2004
Turnover	£87.2m	£122.7m
Operating profit	£2.9m	£(50.9m)
Add back exceptional costs	nil	£52.4m
Business performance	£2.9m	£1.5m

Primecare Primary Care continues to improve its profitability in spite of a reduction in turnover from £72m in the previous year to £52m, following the decision by many PCTs in the new market environment not to outsource their out-of-hours service. The business has focused on improving its operational efficiency and service to ensure it is well placed when contracts are due for renewal and new opportunities present themselves. The recent White Paper on Out of Hospital Care encourages the input of the private sector, which should benefit our business in the longer term. In the meantime, proposals for a major restructuring of PCTs and Strategic Health Authorities have created considerable

uncertainty in hospital planning and this has led to the extension of a number of Primecare's contracts, many of which were due for renewal in the spring of this year.

Forensic Medical continues to perform to expectations with a number of contract extensions secured in the Police business as other Police Authorities continue to consider the prospect of outsourcing their medical provision.

The other major factor in Primary Care's turnover reduction is the ending in August 2005 of NDA's supply of doctors to Atos Origin under the Department of Work and Pensions contract. This was a high turnover, low margin activity for the Group with turnover of £26m in 2004 reducing to £15.5m in 2005. Nestor's staffing business now supplies doctors to Atos Origin, both full time and sessional, on a placement fee basis.

Impact of IFRS

The operating profit figures under IFRS include charges arising from the implementation of IFRS totalling £948k (2004: £46k) analysed as follows:

	2005	2004
IFRS 2, Share-based payments	£425k	£162k
IFRS 3, Amortisation of intangible assets	£344k	£272k
IAS 19, Employee benefits	£179k	£(388k)

All the above charges are non-cash items. The charge for share-based payments is based on a calculation of possible future values of the options granted, but currently all option prices are above the quoted share price.

Cash flow

Closing net borrowings were £79.9m (year-end 2004: £84.6m), with cash flow from operations amounting to £20.9m (2004: £26.7m).

The major feature of working capital management is our control over debtor days outstanding. The year-end figure of 40 days matches that of the previous year but this masks excellent performances in Healthcare Staffing and Social Care where combined debtor days were reduced year on year from 44 to 38 days. In Primary Care, the fundamental change in the customer base from GP practices, most of which paid by direct debit, to PCTs paying monthly accounts, increased debtor days from 35 to 52.

The year's cash flow includes the acquisition of Community Careline Services, a Social Care business, at a cost of £1.7m; together with a further £2.0m deferred consideration in respect of acquisitions made in 2003. There is a further £0.6m deferred consideration payable during 2006, subject to the performance conditions governing its payment.

Renewal of bank facilities

The Group has successfully renegotiated the renewal of its bank facilities, which were due to expire in July 2006. A total facility of £90m has been agreed with a syndicate of three banks to remain in place until December 2009.

Taxation

The tax charge for the year was £3.8m (2004: £2.4m), equivalent to 27% of taxable profit. The underlying tax rate for the Group remains at 30%; savings have been made in 2005 following the successful outcome of settlements and claims from earlier years.

Dividends

The Board is recommending a final dividend of 2.0p per share (2004: 1.5p) payable on 2nd June 2006 to shareholders on the register on 5th May 2006. This is in addition to the interim dividend of 1.0p per share (2004: nil) paid in October 2005.

PCP Joint Venture

In July 2005 we announced the decision of the Department of Health not to proceed with the ISTC project in Basildon. Discussions held over the recovery of bid costs have concluded and the Group will recover the costs incurred up to the point the project was cancelled.

Employees

Delivering an improved operating profit performance when market conditions cause a significant turnover reduction is inevitably an onerous process placing substantial strain upon all involved. Nestor employees, at all levels in the Group, have responded positively and with great resilience to all the challenges presented to them and I thank them for their unstinting hard work. Our staff continue to work with dedication and compassion in their ongoing efforts to deliver quality care to patients and all other service users.

Outlook

The shape of Nestor's business is continuing to change. Prior to 2002 Nestor had a heavy reliance upon the NHS; the strategy in recent years has been to reduce dependency on the NHS by investing in Social Care and improving our performance in *Primary Care*. The result of this strategy is the expectation that, in 2006, flexible staffing to the NHS will contribute less than 10% of Nestor's operating profit.

The outlook for each of the business streams is varied. In Healthcare Staffing, management's approach is to assume that business with the NHS will remain depressed and efforts will continue to focus on other business areas. However, we expect that by maintaining a tight control of the cost base, Healthcare Staffing will remain profitable and cash generative. In Primary Care, the activity base is now stable and the business will continue to demonstrate the quality of its service, enabling it to take advantage of opportunities created when the intentions of the *White Paper on Community Services* come into practice. Social Care remains a buoyant, growing market with current tender activity at very high levels. Nestor's Social Care businesses have the benefit of the pre-eminent position in a very fragmented market, a position we intend to build upon further if suitable acquisition opportunities present themselves.

John Rennocks, Chairman
9th March 2006

Chief Executive's Review

2005 has seen the bedding down of the revised structure implemented in 2004 improving the business units' ability to focus on their respective markets. The reorganisation has been successful and has enabled the Group to report profits (before IFRS adjustments), slightly ahead of last year despite a significant reduction in turnover. The turnover reduction in Primary Care was expected with the completion of the transfer of the responsibility for out-of-hours service to PCTs and the ending of NDA's contract with Atos Origin. The turnover decline in Healthcare Staffing was more than anticipated with the known impact of NHS Professionals ("NHSP") and the introduction of lower pricing under framework agreements being added to by the severe budgetary constraints experienced by Acute Trusts in the final quarter of the year. The revised operating structure, with its lower cost base, has enabled the Group to respond directly to the adverse conditions experienced in Healthcare Staffing, whilst continuing to build the profitability of Social Care and Primary Care.

Business performance

	2005		2004	
	Turnover	Operating profit	Turnover	Operating profit
Healthcare Staffing	£113.1m	£4.3m	£155.1m	£7.4m
Social Care	£108.7m	£12.7m	£112.0m	£11.7m
Primary Care	£87.2m	£2.9m	£122.7m	£1.5m
Total	£309.0m	£19.9m	£389.8m	£20.6m

The operating profits above exclude exceptional items charged in 2004.

Healthcare Staffing

Our Healthcare Staffing businesses provide temporary, locum or permanent staffing solutions to the healthcare market, including NHS trusts, PCTs, private hospitals, nursing and residential homes and industry. Nurses, according to their grade and specialism, are provided through the BNA, Grosvenor and Mayfair brands. Doctors and allied healthcare professionals are supplied through the Medic International, Holt and Pinnacle businesses.

2005 has been a further difficult year in staffing due largely to the budget constraints imposed upon the NHS Acute Trusts, which have exacerbated the effect already established through the volume transferred to NHSP and the pricing pressure from the extension of NHS regional framework agreements. There have been a number of iterations of the framework agreements, which have continued the trend of suppressing margins. With all the original nurse "bank" contracts transferred to NHSP, our

businesses were pleased to be appointed first call providers to NHSP, for shifts they are unable to fill, in two large Acute Trusts. The infrastructure was established locally to ensure the required level of service could be delivered, but unfortunately the volume necessary to make the management of these contracts viable has not materialised due to the budget constraints of the Trusts concerned.

The lack of volume opportunities in the NHS has led to a further rationalisation of our network to a total of 33 branches, whilst still retaining a national presence. It also heightens the necessity for our businesses to focus on developing other avenues of activity which have not to date been effectively pursued. Private hospitals, nursing homes, care homes, community healthcare, prisons and industry all offer opportunities for flexible, cost effective staffing solutions, as indeed do the recent privately managed "treatment centres".

The supply of doctors and allied healthcare professionals through our medical services businesses has also been affected by budgetary constraints and the extension of framework agreements. In addition, with the scaling back of the number of teaching posts in the NHS, there has been a surplus of resource and a consequential reduction in demand for temporary staff, particularly junior hospital doctors.

Social Care

The Social Care businesses provide managed services in the community to support the quality of life for those individuals in need of personal care, primarily in their own homes. Services are commissioned by Local Authorities and PCTs, or purchased by a private individual.

The market for the provision of care for individuals in their own home continues to grow with more than 3 million hours of care undertaken every week in the UK. With people living longer and the desire from all parties involved to enable individuals to lead their lives as independently as possible, the growth in demand for these services will continue. Since the early 1990's Local Authorities have consistently increased the proportion of these services provided by the private sector. By 2004, 69% of such care was outsourced to the independent sector.

Prior to 2004, our Healthcare Staffing and Social Care businesses operated together from the same locations. The branch structure was reorganised in 2004 defining branches as either providers of staffing or social care to better recognise the difference between the requirements of the respective customer bases. Most often a "staffing" requirement is for a specific type of clinician, at short

" Strategically our Primary Care and Social Care businesses are well placed to support the Government's White Paper on community health and care services."

notice, often on the same day and for a short period of time. A social care opportunity usually involves a thorough needs assessment leading to a specific care package for an individual, which could be provided over a lengthy period of time. Our Social Care network extends to 123 owned branches together with a similar number franchised through our Carewatch operation. This remains the largest and most comprehensive national network of any care provider in the UK.

In the first half of 2005 our Social Care business had a significant number of material contracts due for renewal. We reported at the half-year that we had withdrawn from one very large contract where we had been providing very good quality service for a number of years, due to the extremely onerous terms embodied in the revised contract. The penalty clauses were such as to make the business proposition unviable. In addition, two further guaranteed hours contracts were lost to new providers purely due to their lower price position.

The position in the second half of the year has markedly changed. We refer in the Chairman's statement to a "fine tuned approach" to contract tendering. Local Authorities have inevitable pressures on their budgets but this can vary substantially, even between neighbouring authorities. Good local input and market intelligence is therefore essential to the tender process to understand the key criteria, which will drive the decisions of the purchasing body within the Authority. Price competition is equally variable and whilst, where necessary, we have slightly lowered prices to win new business, our operational efficiency and business mix has resulted in an overall margin improvement from 10.4% in 2004 to 11.7% this year.

The bulk of our Social Care business is transacted through the Goldsbrough and Medico brands, both of whom have extensive branch networks. This is important not only to establish and build local relationships with our customers, but also to be accessible to careworkers, those we wish to recruit and those it is important to retain. The Medico network incorporates the majority of the acquisitions made in Social Care since 2002. In 2005 we made just one acquisition, Community Careline Services, which brings a further eight branches across England providing a total of 5,000 hours of care per week.

Our franchise business, Carewatch, which is wholly dedicated to domiciliary care, currently operates from 126 franchise territories. We have extended the Carewatch network in the year and seen good organic growth with franchisees being rewarded for their dedicated approach to developing close working relationships with Local Authorities and their careworkers.

Country Cousins and Patricia White's act as introductory agencies providing personal homecare services for the elderly, through the provision of careworkers and live-in companions. Both businesses had a very successful 2005 and have excellent reputations with their client base leading to most new opportunities being created through word-of-mouth recommendations. New Horizons focuses exclusively on learning disability where the care provided can be highly intensive. These areas of specialist support and care are seen as important growth opportunities for the Group.

Primary Care

Primary Care comprises Primecare Primary Care and Primecare Forensic Medical Services (FMS). Primecare Primary Care provides unscheduled care and out-of-hours services to Primary Care Trusts (PCTs) and GPs; Forensic Medical delivers care in secure environments and to Police Authorities.

The significant reduction in turnover in Primecare Primary Care, from £72m to £52m, was expected following the transfer of contracts to PCTs. The ongoing business is contracted with 45 PCTs, with the major concentrations being in the North East, the Midlands and South Wales. Our service to these customers has been consistently good, but is always most seriously tested over the critical Christmas and New Year period. Primecare's operations were robust and delivered a high standard of service throughout the period with record response times being achieved. We firmly believe that this performance is amongst the best, if not the best, being delivered by any provider. Primecare's service levels have prompted a number of discussions with existing PCT customers over additional services that could be delivered both in-hours and out-of-hours. These include pharmacy and dentistry, as well as the operation of walk-in centres.

Many of Primecare's contracts were due for renewal in the spring of 2006. In the event many have already been extended, in part due to the excellent service, but also due to the uncertainty surrounding the future structure of PCTs, which remains under review. These extensions range from a few months up to two years, but provide the business with certainty over 2006 and a longer period of time to demonstrate the capability of its service provision.

Despite the loss of turnover, Primecare Primary Care recorded a healthy profit in the year due to strong control over its cost base, particularly doctor cost, where the overall cost per hour has been steadily reduced. The management of doctors has improved due to better, and earlier, planning of rotas and through a much reduced use of agencies, which previously were an expensive, last resort option to fill a shift.

Chief Executive's Review continued

The operational structure of the business is now well established through a network of small local call centres supported by the Birmingham Clinical Response Centre, which provides an effective back-up to the local centres as well as retaining the capacity to increase the level of call handling.

Forensic Medical had mixed fortunes in 2005. The Police business substantially increased profitability due to the benefit of contracts won in 2004 and early in 2005 in Leicestershire and Nottinghamshire. The contract with Hampshire Police was extended during the year and there continues to be a wider interest amongst Police Authorities to more actively consider the use of private providers for their medical services. Primecare FMS has been proactive in the introduction of more nursing resource in support of doctors to provide a more flexible and cost-effective service and the prospects remain good for more contract wins in the future. As expected, with very little developmental activity in prison infrastructure, there have been few growth opportunities in the Secure part of Primecare FMS. Nevertheless the ongoing business remains very profitable with good service characteristics, which will be of benefit when opportunities arise.

Primary Care, following a number of years of underperformance, is now an established and consistently profitable part of the *Nestor Group with the potential to deliver significant growth in the future*. The recent Government White Paper promotes the acquisition of patients' services "from a broader range of providers within the NHS, voluntary and private sector". This builds upon the concept of PCTs being commissioners of services rather than providers and whilst such changes are always slow to take effect, our belief is that private enterprise will have an equal opportunity to compete in the provision of primary care services.

Strategically our Primary Care and Social Care businesses are well placed to support the Government's White Paper on community health and care services – "Our health, our care, our say" – by offering innovative and integrated services in the community and at home.

Clinical Governance

The Group continues to adopt a robust and comprehensive approach to the identification and management of clinical risk. This process is described more fully in Dr. Bill Holmes' commentary on Clinical Governance. This commitment has been maintained and enhanced in Nestor despite the difficult trading conditions encountered by the Group across much of its business and the time and effort involved in monitoring our performance which represents a significant cost. However we continue to believe that the information generated is an important factor in managing the clinical risk involved in delivering our healthcare and social care services, and ensuring we satisfy our statutory and regulatory obligations.

Stephen Booty, Chief Executive
9th March 2006

Financial Review

These results are the first full year figures to have been prepared in accordance with International Financial Reporting Standards (IFRS). The basis of preparation and certain accounting policies differ from those set out in the Annual Report and Accounts for the year ended 31st December 2004, which were prepared in accordance with United Kingdom accounting standards.

Comparative figures for 2004 have been restated in accordance with IFRS.

Impact of IFRS

IFRS 1, First time adoption of International Financial Reporting Standards, sets out the requirements for companies preparing financial statements under IFRS for the first time and requires the accounting policies to be applied retrospectively. IFRS 1 contains the option to take advantage of certain exemptions to the retrospective application. The Group has applied such optional exemptions as follows:

- The provisions of IFRS 3 – business combinations, have been applied to acquisitions made since 1st January 2004
- The provisions of IFRS 2 – share-based payments, have been applied only to awards made after 7th November 2002
- The accumulated actuarial gains and losses in relation to employee defined benefit pension schemes have been recognised in full at 1st January 2004 and all subsequent movements in the actuarial valuations have been taken through the statement of recognised income and expense

The published operating profit figures include charges arising from IFRS changes of £948k (2004: £46k) analysed as follows:

	2005	2004
IFRS 2, Share-based payments	£425k	£162k
IFRS 3, Amortisation of intangible assets	£344k	£272k
IAS 19, Employee benefits	£179k	£(388k)

IFRS 2 has been applied to all grants of equity instruments after 7th November 2002. The Group issues equity-settled share-based payments to certain employees under the terms of various employee share and share option schemes. Equity-settled share-based payments are measured at fair value at the date of grant and then expensed on a straight-line basis over the vesting period, based on an estimate of the shares that will ultimately vest.

The charge for amortisation of intangible assets, under IFRS 3, relates to the value of contracts acquired through the Social Care acquisitions made since January 2004. The value attributed to the contracts is calculated on the basis of the discounted cash flows expected to be achieved; this value is then amortised over the remaining lives of the individual contracts.

Under IAS 19, the costs of providing pensions under defined benefit schemes are spread over the period during which the benefit is expected to be derived from the employee's services. Pension obligations are measured at the present value of estimated future cash flows and the scheme assets are measured at fair value at the balance sheet date. Actuarial gains and losses and differences between the expected and actual returns are recognised in the statement of recognised income and expense in the year they arise.

Under IFRS 3, goodwill is no longer amortised on a regular basis but instead is subject to annual impairment reviews. Goodwill totalling £8.3m, that had been amortised in 2004, has been added back to operating profit in the restated comparative figures.

The opening balance sheet net asset value, as at 31st December 2004, has been restated under IFRS and as a consequence increased by £1.6m to £31.2m due chiefly to the reinstatement of goodwill amortised in 2004 of £8.3m, the adding back of the proposed dividend of £1.3m and the recognition of pension scheme deficits, net of deferred tax, totalling (£7.8m).

Turnover

Turnover for the Group reduced by 20.7% to £309.0m as Healthcare Staffing continued to feel the effect of the volume transferred to NHS Professionals and the pressure on pricing exerted through the framework agreements. In addition it has become increasingly clear during the year that many Acute Trusts have been operating under severe budgetary constraints. The reduction in Primary Care is as expected with the transfer of the responsibility for out-of-hours services to PCTs. Also in Primary Care, NDA's contract with Atos Origin, for the supply and administration of doctors for disability assessments, terminated at the end of August 2005.

Financial Review continued

Operating profit and margins

Healthcare Staffing's operating profit was affected by the issues mentioned above, with margin reduced to 3.8% from 4.8% last year.

Social Care increased an already strong margin performance to 11.7% from 10.4% in 2004. The margin includes the management service fee (but little turnover) earned in the franchise business, Carewatch, which had an excellent year.

Primary Care improved its performance considerably, recording a profit of £2.9m in the year, following the loss incurred in 2004. The excellent service record of the business provides a good platform for the contract renewals due in the coming year.

Pre-tax profit

Profit before tax, including the impact of IFRS referred to above, amounted to £14.2m, compared to a loss in 2004 of £47.5m, when significant exceptional costs were incurred.

Taxation

The tax charge for the year was £3.8m, compared to £2.4m in 2004 when the value and rate was significantly affected by the exceptional items. The average tax rate on profit in 2005 was 27%, compared to the underlying rate last year of 30%. This improvement follows the favourable settlement during the year of a number of historic issues for which full provision had been made. Excluding these items the normalised rate remains at 30%.

Earnings per share

The basic adjusted earnings per share were 11.7p, compared to the negative figure reported for last year, due to the exceptional items, of (57.1p).

Cash flow and borrowings

Closing net borrowings for the Group amounted to £79.9m (2004: £84.6m) a reduction of £4.7m. Cash flow from operations amounted to £20.9m (2004: £26.7m) with debtors and creditors continuing to reduce in absolute terms with the fall in turnover. Net capital expenditure was £0.4m (2004: £2.6m) with no significant projects undertaken in the year. Capital expenditure is expected to remain below the level of depreciation for the foreseeable future.

Dividends, interest and corporation tax amounted to a net payment of £12.1m (2004: £14.8m).

Equity shareholders' funds

Equity shareholders' funds increased from £31.2m reported in 2004 to £39.2m, the improvement being the retained profit for the year of £8m.

Acquisitions

In January 2005, the Group completed the acquisition of eight social care branches from Community Careline Services Limited at a cost of £1.7m, with potential additional deferred consideration of £0.2m. In addition, deferred consideration of £2.0m was paid in respect of acquisitions made in previous years.

Pensions

In accordance with IAS19, Employment Benefits, the Group is required to compare the market value of its two defined benefit pension funds' assets at the year-end with the actuarial liabilities of those funds. At 31st December 2005, the pension funds' assets amounted to a total of £29.6m (2004: £24.1m) compared with total liabilities of £45.8m (2004: £39.4m), a net aggregate deficit of £16.2m (2004: £15.3m).

Treasury management and financial instruments

Financial instruments include all assets and liabilities of a financial nature such as cash, loans, finance leases, overdrafts and long term liabilities. All such instruments play an important part in the operations of the company to enable it to operate smoothly and efficiently and to pay its obligations as they fall due. They also enable the company to fulfill its investment strategy including making appropriate acquisitions. The company's objective is to use financial instruments to minimise the cost of capital at an acceptably low financial risk and to maximise flexibility to take advantage of investment and acquisition opportunities as they arise.

The Group is primarily a UK Healthcare business and does not have significant exposure to foreign exchange risks. Nevertheless the Group's strategy is to hedge its foreign exchange exposure where it arises with foreign currency loans or forward exchange contracts as appropriate.

The main risks arising from the Group's financial instruments are interest rate and liquidity risks. The Board considers each of these risks on a regular basis and the Group's stance towards each of these risks has remained unchanged.

The Group has recently renegotiated its banking facilities. Under the new arrangement the Group has in place £80.0m of committed borrowing facilities, plus uncommitted overdraft facilities of £10.0m at an initial margin of 1.10% above LIBOR and due for repayment in December 2009. The margin payable can reduce during the term of the facilities if certain performance criteria are met. At the end of the year, the Group had borrowings less cash of £79.9m (2004: £84.6m) and undrawn committed borrowing facilities of £19.0m. It is, and has been throughout the year, the Group's policy that no trading in financial instruments will be undertaken.

Under the previous banking facilities, the Group entered into a hedging arrangement in November 2002 which had the effect of fixing £35m of its borrowing within an acceptable range of interest rates for four years. It is intended that a similar strategy will be followed under the newly established facilities.

Controls

Financial and operational controls remain robust across the Group with considerable attention paid to the control environment and balance sheet management on a monthly basis. A number of new appointments have been made within Finance, which will further improve the overall calibre of the team. The Business Review team continue to be effective in developing business procedures and have introduced a more constructive risk management review process.

Martyn Ellis, Finance Director
9th March 2006

“ We believe our governance processes to be amongst the best to be found in the independent sector.”

Clinical Governance

Health and social care regulation continues to increase. Nestor recognises the direction provided by government, and the consequent demands of our clients that we should further strengthen our processes to improve safety and meet externally set standards. I am pleased to be able to report further progress.

One of the key challenges faced by an organisation with a distributed branch network is maintaining consistency in the application of group procedures. In the last year, Nestor's quality team has been expanded, and we have developed a bespoke quality reporting system. Both add to the efficiency of our reporting, and assure our quality.

Our Primary Care businesses have seen further increases in the regulation of doctors. The expectation of further monitoring of their work has been addressed by a fundamental review of Primecare Primary Care's clinical governance structure which, with the full support of the Board, has been further strengthened and developed. Our aim is to deliver the linked objectives of greater patient safety and improved clinician efficiency. We see no conflict between quality and productivity in clinical activities. For example, patient access to Primecare, a key marker of performance, has steadily improved. We were particularly proud of achievements over Christmas, always a challenging time in unscheduled care; in December 2005, the average patient was able to contact the service in 19 seconds, and when needed, telephone consultations with a clinician were provided on average in 13 minutes. Both figures reflect a performance which comfortably exceeds the National Quality Standards, a performance we believe to be among the best in the country. Measures of patient satisfaction remain very reassuring.

In domiciliary care, our program of branch audits continues to ensure we meet our statutory and regulatory responsibilities, and our intranet-based quality management system will further strengthen our adverse incident reporting.

Independent comparisons are uncommon, but in 2005 a consultancy firm was commissioned by a group of Primary Care Trusts in the Midlands to review unscheduled care services provided in their area by three different providers. Our performance was scored highly, and the improvements achieved over the previous two years received favourable comment.

We believe our governance processes to be amongst the best to be found in the independent sector. Where possible, we always seek to mirror processes found within the state sector, for example within the NHS, in order to deliver efficiency, provide the opportunity to share information, and to allow comparability of structure and performance. We continue to receive the guidance of our Clinical Advisory Board, comprising eminent healthcare practitioners who are independent of the Group.

In each of my previous reports, I have argued that the resources allocated to quality and governance provide control of clinical risk, and add to shareholder value. I remain of that view, and with my fellow directors, continue to see the delivery of safe and accountable services as a central objective which contributes to the success of Nestor.

Dr William Holmes, Group Medical Director
9th March 2006

Employees and Social Responsibility

" The Group continues to refine its systems to capture the diversity of the Group and seeks innovative methods of attracting scarce clinical and carer resource."

Employee involvement

The Group believes that involving its employees in all aspects of its business, particularly the economic and financial factors affecting the Group's performance, is crucial to its future success. It is always seeking ways to improve communication across its businesses, both between its central and operational functions and between the various operations themselves where appropriate.

It is the Group's policy to encourage employees to participate in its success, through a variety of performance-related incentive arrangements, including the provision of savings-related share option schemes.

Internal newsletters are issued regularly, increasingly through the use of new media to reach all staff faster and more efficiently. Its key policies and procedures are published on a Group-wide intranet, which is available to all staff, and the intranet homepage contains relevant and up-to-date information of interest on a real-time basis.

Diversity and training

The Group recognises its responsibilities in this key area of working life and is continually taking steps to balance society and employee needs with its business requirements. It has a wide *and varied employee base with significant numbers of female employees*, many at senior management level, as well as a significant employee base of individuals who come from ethnic minority groupings.

The programme to actively recruit employees with disabilities, particularly in the Birmingham Clinical Response Centre, continued through the year. The Group's operational working practices and policies continue to comply with the Disability Discrimination Act 1995.

The Group continues to refine its systems to capture the diversity of the Group and seeks innovative methods of attracting scarce clinical and carer resource, including the provision of proven computer diagnostic software enabling clinicians to provide clinical advice from their own homes and operational processes to facilitate part time working.

In the Group's staffing businesses, the requirements of legislation, particularly the Care Standards Act 2000, and of its key customers have led to the development of comprehensive training and

development programmes for both employees and the health and care professionals who help to provide the Group's services. These programmes are delivered by a combination of in-house and externally-based training organisations and support the high levels of service offered by the Group.

Health and Safety

The Board is aware of its responsibilities towards its employees and all users of the Group's services in health and safety matters. It recognises its ultimate responsibility for the setting and monitoring of appropriate policies, guidelines and practices in the formal Schedule of Matters Reserved for the Board's consideration.

The Group's Director of Human Resources is directly accountable to the Chief Executive for overseeing safety matters and in 2005 has worked closely with the Group's business units to roll out revised policies and reporting arrangements. Day to day advice is provided by the Group Health and Safety Manager and by an external consultancy.

An ongoing training programme supports the effective implementation of this process which is based on a comprehensive series of risk assessments and reporting arrangements.

During the year all health and safety matters were integrated into the newly-introduced Nestor Quality Management System.

Charity of the Year

As part of its commitment to UK health and social care, the Group asks many of its branches every year to vote for the organisation or charity they would like to support as Charity of the Year.

Throughout 2005, the employees of the Group raised money in many ways for the children's charity *When you wish upon a Star*. This charity, founded in 1990, has the sole aim of granting wishes to children with life threatening and terminal illnesses.

The Group is always looking for new ways in which to involve its employees in the communities in which they are based. A number of successful programmes were run throughout 2005. Throughout the UK, the Group's branches regularly support charities pertinent to their own locality or business sector, as well as the Charity of the Year.

Employees and Social Responsibility continued

The FTSE4Good Index

The London Stock Exchange periodically invites limited companies to be listed on FTSE4Good indices. These provide benchmarks against which institutions can measure and market the performance of socially responsible funds. The initiative is formed in conjunction with UNICEF (United Nations Children's Fund) and all licensing fees from the fund are donated to UNICEF.

Developed in association with EIRIS (the Ethical Investment Research Service), FTSE4Good is a series of indices consisting of both a trackable and a benchmark index. They are designed as a first step towards setting a global standard in the fast growing area of socially responsible investment (SRI).

As a reflection of the services that we deliver the Group has been listed on the FTSE4Good index.

Business in the Community

BITC is the UK's longest established business-led charity that delivers programmes designed to make a positive impact on society. As an employee champion the Group is directly involved with projects which address issues for the "unqualified" workforce. Employee champions work through issues and make recommendations on key national strategic directives such as *workforce capacity recommendations for the recruitment and retention of social care workers*.

Training programmes aimed at, for example, refreshing study skills, giving individuals confidence and interview techniques are designed to provide the workforce with the ability to progress within their chosen work environment.

Skills for Life

The Department for Education and Skills (DfES) has invited the Group to participate and promote the 'Skills for Life' programme. Within many workforce population groups there is a recognised lack of basic skills in literacy and numeracy. These gaps are being closed through projects enabled by budget investment from the European Social Fund. Local projects run under the programme are those such as the Great Yarmouth scheme and the Workers Education Association scheme in Hertfordshire and Essex.

Action for Carers and Employment (ACE) National Project

The Group works with the Action for Carers and Employment (ACE) National partnership project to formulate

recommendations for practical, workable solutions for carers. The project supports the inclusion of carers in work opportunities and is funded by the European Social Fund's Equal Programme with a budget in excess of £100m.

The UK's 6 million carers look after partners, relatives and close friends in need of help because they are ill, frail or have a disability. More than half of the nation's carers currently have to balance paid work and care, and are unpaid as carers. It is crucial that good care services are available to those in need of care to enable carers to continue in work, either from necessity or from choice.

Environmental policy

As a service-based organisation, with no manufacturing, limited transportation facilities and no freehold properties, the Group's exposure to environmental risk is limited, as is its ability to control the environmental impact of its activities.

However, the Group and its businesses are committed to following the best environmental practices in the day-to-day conduct of their business and the management of their resources and facilities. During the year, the Group continued to refine the formal environmental policy adopted by the Board in 2000, with a particular focus on matters relating to the clinical services provided by the Group. The policy document, which is directed at minimising the potential impact of the Group's operations on the environment, provides that the Group's Board retains ultimate responsibility for setting and monitoring its policy on environmental matters.

The policy provides for the promotion of an understanding of environmental consideration across the Group and all managers are directed to encourage staff to follow the good practice outlined in the policy at all times.

The aims of the Group's environmental policy are:

- to take all practical steps to ensure the Group's business activities have the minimum negative impact on the environment
- to achieve the most economic and careful use of sources of fuel and energy
- to minimise the production of waste and to manage the disposal of clinical waste in a safe manner
- to make the maximum practical use of recycling.

Responsibility for the coordination of the policy throughout the Group rests with the Board, with the Chief Executive having specific responsibility. The policy is administered by the Group's Director of Human Resources, who coordinates the activities of various relevant Group functions.

Specialist advisors are appointed by the Director of Human Resources *as required to ensure that best practice is followed*, that the Group is aware of potential opportunities to improve performance and that all legislative and statutory requirements are met.

The managing directors of the Group's operating companies are responsible for ensuring compliance with the policy. Where appropriate, departmental representatives or coordinators have been appointed to act as a focal point for the dissemination of information and the promotion of initiatives to improve the immediate environment, reducing waste and ensuring that the objectives of the policy are met. Where practicable, paper and other consumables are recycled and all employees are encouraged to operate the business in as environmentally-friendly a manner as possible.

Ethical matters

The Board has adopted a formal Code of Business Conduct, covering all the businesses in the Group, which has consolidated all of the various codes previously applicable to them. The Code provides comprehensive guidelines to all employees and "members" as to the standard of business ethics expected from them as representatives of the Group. It also recognises the importance to the Group of operating to the highest possible ethical standards, bearing in mind the nature of the services offered by Group companies and the needs of their clients.

The Group operates two comprehensive whistleblowing policies, in respect of clinical issues and general operational and financial matters.

At the Group's Business Resource Centre in Hatfield, most gifts received by members of staff from suppliers and potential suppliers are auctioned amongst all staff (where practicable) and the proceeds of such auctions are donated to the Group's Charity of the Year.

All senior managers are required to declare, on an annual basis, any hospitality received during the year in their capacity as employees of the Group and to disclose any interests they may have in connected or competing organisations. These declarations are monitored by the Group Company Secretary and reported to the Board at the end of each year.

All Board members are required, once a year, to submit their annual expense claims to the scrutiny of the entire Board.

David Collison, Group Company Secretary
9th March 2006

Board of Directors

1 John Rennocks

Chairman

(60), joined the Group and was appointed to the Board as Chairman in October 2003. A chartered accountant, he is also non-executive chairman of Diploma plc and holds a number of non-executive appointments in a broad range of companies including Inmarsat plc, Foreign & Colonial Investment Trust plc, Babcock International Group plc and Wagon plc.

Previously, he was Executive Director, Finance of Corus Group plc (formerly British Steel plc) between 1996 and 2001. From 1989 to 1996 he was Finance Director of Powergen plc and prior to that Finance Director and Company Secretary of Smith & Nephew plc.

He is Chairman of the Board's Nomination Committee and a member of its Audit and Remuneration Committees.

2 Stephen Booty

Chief Executive

(51), was appointed to the Board as an Executive Director in June 2002, having joined the Group in January 2002, as Managing Director, Healthcare Personnel Division. He was appointed Acting Chief Executive in May 2004 and Chief Executive in December 2004.

He has over twenty years experience in the fast moving consumer goods sector, working for blue chip organisations, marketing branded goods and driving efficiencies through innovative business processes. His previous roles include Chief Operating Officer, Europe at Chep International and senior sales, management and operational roles at Kimberly-Clark and Scott Paper.

3 Martyn Ellis

Finance Director

(49), joined the Group and was appointed to the Board in May 2003. A cost and management accountant, he previously held positions as Finance Director of TeleCity plc, Whitecroft plc, Mann Egerton and Campbell Foods (UK).

4 Roger Dye

Non-Executive Director

(54), was appointed to the Board as a non-executive director in January 2004. A chartered accountant, he was Finance Director of the Davis Service Group Plc since August 2000 and became its Chief Executive in May 2005. A UK public company director since 1987, he has been Group Finance Director of Transport Development Group plc, Cray Electronics plc and Domino Printing Sciences plc.

He is Chairman of the Board's Audit Committee and serves on its Nomination and Remuneration Committees.

5 Dr William Holmes

Executive Director

(51), was appointed to the Board as a non-executive director in January 2000 and as the Group's executive Medical Director in October 2001. His executive responsibilities include the developing and monitoring of clinical standards and leading a team to provide clinical governance across the Group. He is a Fellow of the Royal College of Physicians of London and a Fellow of the Royal College of General Practitioners. In addition to his corporate responsibilities, he continues to undertake regular clinical sessions in occupational medicine.

6 Sir Andrew Foster

Non-Executive Director

(61), was appointed to the Board in January 2004. He has had a long and distinguished career in public service, having served as Chief Executive of the Audit Commission for England & Wales between 1992 and 2003. Other previous appointments include Deputy Chief Executive of the NHS and Director of Social Services for North Yorkshire County Council. He is now Deputy Chairman of the Royal Bank of Canada Europe Ltd., a non-executive director of the Sports Council and has a range of positions in the public and private sectors.

He is the senior non-executive director and Chairman of the Board's Remuneration Committee. He is also a member of its Nomination and Audit Committees.

7 Ingrid Alexander, CBE

Non-Executive Director

(54), was appointed to the Board in August 2001. An independent management consultant, she was the final Chairperson of the Central Council for Education and Training in Social Work and a member of the Kings Fund Grants Committee. She was appointed to the Board of the Social Care Institute for Excellence in 2005. She is a former member of the General Social Care Council Advisory Group and the Strategy Group for the NHS Chief Executive's leadership programme and has worked widely with a number of other organisations in the health and social care field. Previously, she was Assistant Director for Resources at Birmingham City Council.

She is a member of the Board's Nomination, Audit and Remuneration Committees.

Directors' Report

The directors are pleased to present their report and the audited financial statements for the year ended 31st December 2005.

Principal activities, results and future developments

Nestor Healthcare Group plc is the holding company of a group of companies in the healthcare sector. Its principal activities are organised into three business units. These comprise:

- Healthcare Staffing – the provision of nurses and carers, locum doctors and other medical personnel;
- Social Care – the provision of home and social care personnel and services through a network of company owned and franchise branches across the UK; and
- Primary Care – the provision of GP and other out-of-hours services to the NHS and the provision of healthcare and related services to Police Authorities and secure institutions.

The Chairman's Statement, Chief Executive's Review and Financial Review on pages 1 to 9 provide a report on the Group's activities, trading results and future developments.

Results and dividends

The profit attributable to shareholders was £10,251,000 (2004: loss of £50,010,000). An interim dividend of 1.00 pence was paid in October 2005 following payment of the 1.50 pence final dividend for 2004 in June 2005. The total dividend paid, representing these combined dividends of 2.50 pence, was £2,190,000.

The directors now recommend a final dividend of 2.00 pence per ordinary share, to be paid to shareholders on 2nd June 2006.

Post-balance sheet event

Since the balance sheet date the Group has renegotiated the renewal of its bank facilities, which had been due to expire in July 2006. A total facility of £90,000,000 has been agreed with a syndicate of three banks to remain in place until December 2009. Borrowing under this facility is secured by a charge created over Group assets.

Directors

The directors who served during the year were Ingrid Alexander, Stephen Booty, Roger Dye, Martyn Ellis, Sir Andrew Foster, William Holmes and John Rennocks. All the directors served throughout 2005.

In accordance with the Articles of Association, John Rennocks, Roger Dye, Sir Andrew Foster and Ingrid Alexander will retire by rotation at the Annual General Meeting and, being eligible, will offer themselves for re-election.

Stephen Booty, Martyn Ellis and William Holmes each has a service agreement with the Company, further details of which are provided at page 22 in the Remuneration Report.

Directors' interests

All directors' interests, including details of shareholdings, are set out in the Remuneration Report of the Board on pages 21 to 25.

Substantial shareholdings

At the date of this report the Company has been notified of the following material interests of 3% or more and non-material interests of 10% or more in its ordinary share capital:

Shareholder	Number of shares	Percentage of Issued share capital
Schroder Investment Management Limited	22,534,770	25.72%
Aberforth Partners LLP	10,350,000	11.81%
M & G Investment Management Limited	3,805,660	4.34%
SVG Investment Managers Limited	2,995,290	3.42%

Details of the authorised and issued share capital of the Company during the year ended 31st December 2005 are given in note 21 to the financial statements.

Secretary

Emma Thomas left the Group's employment and resigned as Group Company Secretary on 11th March 2005, being replaced by David Collison from the same date.

Registered office

On 1st February 2006 the address of the registered office of the Company was changed to that of the new corporate head office at Allen House, Station Road, Egham, Surrey, TW20 9NT.

Country of incorporation

The Company is incorporated in Great Britain and registered in England and Wales.

Annual General Meeting – special business

The Annual General Meeting of the Company will take place at Allen House, Station Road, Egham, Surrey TW20 9NT on Thursday, 27th April 2006 at 12.00 noon. The notice of the Annual General Meeting may be found in the Notice of Meeting accompanying this Report. In addition to the routine business of the meeting, the following special business will be transacted:

- **Directors' authority to issue shares (Resolution 9)**

The Companies Act 1985 ("the Act") prevents directors from allotting unissued securities without the authority of shareholders. In certain circumstances this could be unduly restrictive. The proposed resolution will give the directors a general authority to issue shares of the Company for cash, within certain constraints, without complying with the statutory pre-emption procedures. The total number of relevant shares that the directors will have the authority to allot will be 8,300,000 ordinary shares of 10p each (representing 9.5% of the share capital currently in issue). The directors have no present intention to exercise this authority (except in relation to the allotment of shares under the Group's share option schemes). The authority in Resolution 9 will expire at the conclusion of the next Annual General Meeting or on 27th July 2007, whichever is the earlier.

- **Adoption of the rules of a performance share plan (Resolution 10)**

The Remuneration Committee of the Company considers that it would be advantageous for the Company to change the current incentive policy for senior executives. It is proposing to discontinue the existing annual bonus and long-term incentive arrangements and replace them with a new annual bonus plan and Performance Share Plan. The Performance Share Plan will provide for conditional awards of shares worth up to 100% of base salary, which would vest after three years subject to a sliding scale of total shareholder return performance against the companies comprising the FTSE Small Cap Index, measured over a three year period. The Committee considers that this proposal simplifies the Company's incentive arrangements for senior executives whilst providing a clear focus on encouraging superior total shareholder return. Resolution 10 will be put to the Annual General Meeting as an ordinary resolution to seek approval of the rules of the Performance Share Plan.

A copy of the draft rules of the Nestor Healthcare Performance Share Plan will be available for inspection at New Bridge Street Consultants LLP, 20 Little Britain, London EC1A 7DH during normal business hours on any weekday (Saturday and English public holidays excluded) until the close of the Annual General Meeting and at the place of the Annual General Meeting for at least 15 minutes prior to and during the meeting. The Plan and its rules are also described in further detail in the accompanying circular to shareholders.

- **Restricted disapplication of pre-emption rights (Resolution 11)**

The proposed special resolution will give the directors a limited authority to issue equity shares for cash other than to existing shareholders in proportion to their existing shareholdings notwithstanding the pre-emption provisions of Section 89 of the Act. This limited authority would allow the directors to make such issues provided they do not exceed in aggregate an amount equal to 5% of the issued share capital of the Company. The resolution also contains provisions enabling the directors to take action to overcome certain practical difficulties that could arise in the case of a rights issue. The authority in Resolution 11 will expire on the conclusion of the next Annual General Meeting or on 27th July 2007, whichever is the earlier.

- **Purchase by the Company of its own shares (Resolution 12)**

The directors consider that it would be advantageous for the Company to renew for a further year the existing authority granted at last year's Annual General Meeting, to allow the use of the Company's available cash resources to acquire its own shares in the market for cancellation. This authority is granted pursuant to Section 162 of the Act.

Accordingly, a special resolution is proposed to authorise the purchase in the market of up to 10% of the issued ordinary shares of the Company at a price of not more than 105% of the average of the middle market quotations for the ordinary shares of the Company (as derived from the London Stock Exchange Daily Official List) for the ten business days prior to the date of purchase.

The directors do not intend to exercise the Company's power to purchase its own shares other than in circumstances where they consider this to be in the shareholders' interests and where this would result in an increase in earnings per share. They have no present intention to exercise this authority.

Charitable and political donations

No political donations were made during the year (2004: £nil). Charitable donations of £2,200 were made to various charities in 2005 (2004: £3,600).

Taxation status

The Company is not a close company within the meaning of the Income and Corporation Taxes Act 1988.

Disabled employees

It is the Group's policy that disabled persons should be considered for employment, training, career development and promotion on the basis of their abilities and aptitudes in common with all employees.

The Group applies employment policies that are fair and equitable for all employees and which ensure that entry into and progression within the Group are determined solely by application of job criteria and personal ability and competency.

Directors' Report continued

Full and fair consideration (having regard to the person's particular aptitudes and abilities) is given to applications for employment and the career development of disabled persons. The Group's training and development policies make it clear that the Group will take all steps practicable to ensure that employees who become disabled during the time they are employed by the Group are able to continue to perform their duties.

Employee involvement

The Group attaches considerable importance to ensuring that all its employees are provided with information concerning them as employees, particularly the economic and financial factors affecting the Group's performance and the market in which the Group operates. Involvement of employees in the Group's performance is also encouraged by the availability of performance-related bonuses as well as share option schemes, which are described in more detail elsewhere in this report.

Internal circulars and newsletters are issued on a monthly basis and consultation between management and staff is an ongoing process. Employees are consulted on issues directly affecting them wherever practicable. Further details of the Group's policies and practices relating to employee involvement may be found on page 11 to this report.

Creditor payment policy

It is the Group's policy to have appropriate terms and conditions for transactions with suppliers, ranging from standard terms and conditions to those which have been specifically negotiated, and that in the absence of dispute, payment will be made in accordance with those terms and conditions and conforming to the CBI Code of Best Practice; copies are available from the CBI at Centrepont, 103 New Oxford Street, London. At 31st December 2005 trade creditors represented sixteen days' purchases (2004: eleven days).

The directors' reports of the Group's United Kingdom operating companies give information about their creditor payment policies as required by the Companies Act. The Company, as a holding company, does not itself make any relevant payments in this respect.

Auditors

A resolution proposing the reappointment of PricewaterhouseCoopers LLP, Chartered Accountants, as auditors to the Company and authorising the Audit Committee of the Board to determine their remuneration will be put to the Annual General Meeting.

Approved by the Board on 9th March 2006 and signed on its behalf by:

David Collison
Group Company Secretary



Nestor Healthcare Group plc
Registered number 1992981

Directors' Responsibilities

In respect of the preparation of financial statements:

The directors are required by company law to prepare financial statements which give a true and fair view of the state of affairs of the Company and the Group at the end of the financial year and of the profit and cash flows of the Group for the period to that date.

The financial statements must be prepared in compliance with the required formats and disclosures of the Companies Act 1985 and in accordance with applicable accounting standards. In addition, the directors are required:

- to select suitable accounting policies and apply them consistently;
- to make judgements and estimates that are reasonable and prudent;
- to state that the financial statements comply with International Financial Reporting Standards;
- to prepare the financial statements on a going concern basis unless it is inappropriate to presume that the Company will continue in business.

The directors confirm that the financial statements comply with the above requirements.

The directors are also responsible for the maintenance and integrity of the Nestor Healthcare Group plc websites on which the financial statements are published. Legislation in the United Kingdom governing the preparation and dissemination of financial statements may differ from legislation in other jurisdictions.

The directors are also responsible for maintaining adequate accounting records so as to ensure that the financial statements comply with the requirements of the Companies Act 1985, for safeguarding the assets of the Group, and hence for preventing and detecting fraud and other irregularities.

Remuneration Report

The Board is pleased to present its remuneration report for the year ended 31st December 2005.

Remuneration Committee (non-audited)

During the year, the Board delegated its powers to determine the Company's remuneration policy for senior executives, including executive directors, to the Remuneration Committee ("the Committee"), the members of which during the year were Sir Andrew Foster (Chairman), Ingrid Alexander, Roger Dye, all of whom are regarded by the Board as independent non-executive directors and John Rennocks (who was regarded by the Board as being independent within the meaning of the Code, on the date of his appointment). The Board has retained responsibility for setting the remuneration of the Company's Chairman since he currently serves as a member of the Committee.

The terms of reference of the Committee may be found on the Company's website. Further details relating to the Committee may be found on page 27 of this report.

In determining its policy, the Committee has paid regard to the principles and provisions of good governance contained in the Code on Corporate Governance published in July 2003 ("the Code") and to the Directors' Remuneration Regulations 2002. It has also received advice on executive remuneration from New Bridge Street Consultants LLP ("NBSC"), which during the year was retained by the Committee as its regular advisor. A copy of a statement relating to the terms on which NBSC is engaged by the Committee is available on the Company's website. The Committee has also received assistance from Stephen Booty, the Group's Chief Executive and James Buchanan, the Group's Director of Human Resources, both of whom attend meetings of the Committee as required but not in respect of matters relating directly to their own remuneration.

The Company has also instructed NBSC to advise it on certain ad hoc matters during the year, for example in relation to the administration of the Company's share schemes.

Remuneration Policy (non-audited)

The Committee's overall aim is to provide a package of remuneration which:

- is sufficient but no more than is necessary to attract, retain and motivate all of the Company's most senior management, including executive directors;
- rewards good performance with remuneration that is in line with that payable in broadly comparable businesses; and
- rewards exceptional performance in such a way as to align the executives' interests with those of the Group's shareholders.

To that end, the Committee structures executive remuneration in two distinct parts: fixed remuneration of basic salary and benefits and variable performance-related remuneration, in the form of a cash bonus and long-term incentives. Remuneration is structured so that the variable pay element forms a significant portion of each director's package.

Basic salary and benefits

Basic salary is determined by reference to the responsibilities and performance of the individual directors during the year, taking into account experience and the rates of basic pay for similar roles in comparable companies. The Committee's overall aim is to ensure that the basic salary paid to the Group's senior executives is broadly in line with the median of that paid by comparable businesses, having particular regard to their size and complexity. Salaries are reviewed annually, normally in November or December of each year and any adjustments usually take effect from 1st January in the following year. It is the Committee's practice to undertake formal market benchmarking of directors' and senior executives' salaries, with the assistance of NBSC, every two years. With effect from 1st January 2006, executive directors' basic salaries will range from £164,800 to £312,000. The Company additionally provides a range of benefits to executive directors, the most significant of which are a fully expensed car or cash alternative and pension benefits (full details of which are set out below).

Cash bonus

Each year, the Committee sets stretching bonus targets for each executive, aiming to achieve a balance between short and medium-term objectives. In 2005 and 2006, targets comprise overall Company performance criteria relating to profit before tax. No bonus is payable if the relevant financial targets are not met.

The maximum such annual bonus payable to executive directors is 80% of salary, except that payable to William Holmes, which is 50% of salary. Directors who are eligible to receive a maximum annual bonus of 80% are required to invest one half of their post-tax receipt into the Company's Long Term Incentive Plan ("LTIP"). Details of the LTIP are provided later in this report. Bonuses are not pensionable.

Long-Term Incentives

The Company currently operates two long-term incentive schemes, the Nestor Healthcare Group Share Option Plan 2002 ("the 2002 Plan") and the LTIP, both of which were adopted following approval by shareholders in 2002. In proposing the schemes, the Committee took extensive advice from NBSC, sought and obtained the prior approval of a number of the Company's largest shareholders and complied with prevailing best practice relating to such arrangements.

Remuneration Report continued

i. The 2002 Plan

The Committee believes that share ownership by senior executives is an effective means of rewarding superior performance, since the interests of management and shareholders are thereby aligned. The Committee further believes that the provision of share schemes to the Group's managers should be structured in such a way as to encourage them to achieve the Group's long-term aims and that the Group's most senior managers, including executive directors, should be rewarded for exceptional performance with potentially significant rewards.

It is generally the Company's policy, therefore, to grant share options regularly, on a tiered basis, to a broad range of middle and senior management, including executive directors. Generally (though not in 2004) options have been granted annually to executive directors, to a value equivalent to one times salary, although in exceptional cases, where a key executive joins the Group, a higher limit has sometimes been applied. In other years, a lower limit has also been applied. In 2005, 1,559,057 share options were granted under the 2002 Plan.

"Normal" options

For "normal" options granted to the Group's most senior executives, including all executive directors, a range of normalised earnings per share ("EPS") performance targets will apply to grants as shown below:

	Average growth required in EPS
1st third of an option	RPI + 5% pa
2nd third of an option	RPI + 6% pa
Final third of an option	RPI + 10% pa

In all cases, performance is tested over a three-year period. Since January 2004, the Committee has resolved that there will be no opportunities to re-test performance for grants made after that date.

EPS was chosen as the relevant benchmark for the measurement of the Company's performance since the target requires substantial improvement in underlying financial performance before options may be exercised. This complements the requirement inherent in an option, which is to grow the share price. The range of EPS targets are considered to be appropriately stretching, generating higher potential reward levels for higher levels of financial performance. This benchmark will continue to be kept under review.

All of the 1,559,057 options granted during the year under the 2002 Plan were "normal" options.

"Super" options

In addition to "normal" options, the 2002 Plan also provides for the grant of "super" options to certain of the Group's most senior managers, including executive directors. The Committee does not intend to grant these "super" options to those executive directors who are eligible to receive LTIP awards but may grant such options to William Holmes, who is not. These options may be granted over shares worth up to one and a half times the individual's salary and the exercise of these options is subject to the achievement of more stretching targets than those prescribed by the Committee in relation to "normal" options.

Performance targets relating to "super" options involve a comparison of the Company's total shareholder return ("TSR") with companies in the FTSE Mid 250 index (excluding investment trusts) as at the date of grant, measured over a single three year period from grant. Options are exercisable as set out below:

Nestor's TSR ranking in group	% of "super" options exercisable
Below 45th percentile	0%
45th percentile	40%
45th percentile to 25th percentile	Sliding scale from 40% to 100%
25th percentile and above	100%

In addition to the TSR condition above, no element of the option is exercisable unless the Company's EPS growth over the three-year period exceeds 5% per annum over RPI. There is no opportunity to re-test performance.

No options were granted during the year under this scheme.

ii. The LTIP

Under the LTIP, the executive directors who are eligible to participate (namely Stephen Booty and Martyn Ellis) are required to invest one half of their post-tax cash bonus in buying shares in the Company. The investment will be matched by the grant of matching awards.

Matching awards will normally only vest on the third anniversary of their grant if the participant is still in the Company's employment, has retained the shares purchased with the bonus and if specified performance targets are met. The current performance target involves a comparison of the Company's TSR with companies in the FTSE Mid 250 index (excluding investment trusts) as at the date of grant, measured over a single three year period from grant. Matching awards vest as set out below:

Nestor's TSR ranking in group	Matching Ratio	
	Chief Executive	Other Eligible Executive Directors
Below 45th percentile	0	0
45th percentile	0.5:1	0.3:1
45th percentile to 10th percentile	Sliding scale from 0.5:1 to 4:1	Sliding scale from 0.3:1 to 2.5:1
10th percentile and above	4:1	2.5:1

In addition to the TSR condition above, none of the award will vest if the Company's EPS growth does not exceed the growth in RPI by an average of at least 5% per annum over the three year period. There is no opportunity to re-test performance.

The Committee considers TSR to be a suitable performance measure for both the "super" options and the LTIP as it clearly aligns interests of shareholders and executives. It also considers that the FTSE Mid 250 Index is an appropriate benchmark as there are no other companies with a similar business profile to the Company listed on the UK Stock Exchange. TSR performance will be independently calculated for the Committee. A chart showing the Company's TSR compared to the FTSE Mid 250 Index over the last five financial years is shown below.

Participation in the matching awards to date has been as follows:

	Notionally awarded in 2004	Share price at date of notional award (p)	Lapsed in 2004	Notionally awarded in 2005	Share price at date of notional award (p)	Lapsed in 2005	Potential interest in shares at 31.12.05	Amount charged against profit in 2005 £000
Stephen Booty	33,108	185.0	—	107,559	148.75	—	140,667	29
Martyn Ellis	22,297	185.0	—	51,093	148.75	—	73,390	16
Justin Jewitt	54,054	185.0	(54,054)	—	—	—	—	—
Stephen Page	15,589	185.0	(15,589)	—	—	—	—	—
Total directors	125,048		(69,643)	158,652		—	214,057	45

Earliest vesting dates for awards made in 2004 and 2005 are 7th April 2007 and 11th May 2008, respectively.

iii. SAYE Scheme

The Company also operates a savings related share option scheme, which provides a long-term savings opportunity for all of the Group's employees, as well as encouraging them to participate in the success of the Company. Participation is open to all permanent employees who are able to make regular monthly savings and are exercisable in normal circumstances after three or five years at a price which is fixed at a discount of 20% from the average of the mid-market prices for the five business days immediately preceding the date on which invitations are made by the Committee. In 2005 options over 515,121 shares were issued under this scheme.

iv. Share Price Linked Scheme

In December 2004, the Company established a phantom long-term incentive arrangement for the benefit of the Chief Executive, designed further to align his interests with those of the Company in the light of the significant challenges presented by the changes in the market in which the Company now operates. The scheme provides for the grant of 477,137 notional "phantom" options over the Company's shares, which are exercisable in up to two equal tranches, provided the Company achieves challenging profit before tax targets in 2005 and 2006 respectively, at any time after the performance conditions have been met before 14th December 2007. The maximum amount payable under this scheme to the Chief Executive is £500,000 and the value of the award is entirely dependent upon an increase in the Company's share price from the exercise price, the prevailing mid-market price at the date of grant being 125.75 pence.

The required profit before tax target for 2005 was not in fact achieved.

Remuneration Report continued

Company policy on the pensions of executive directors (non-audited)

Until it was closed to new entrants in April 2003, executive directors were able to join the Nestor Healthcare Group Retirement Benefits Scheme ("the Scheme"), a funded, Inland Revenue approved, final salary occupational pension scheme. Pensions in the Scheme are based on final salary (excluding bonuses) and length of pensionable service. In respect of those directors who are members of the Scheme, the Company has agreed to provide benefits based on their actual basic salary, even where this exceeds the Inland Revenue Earnings "cap", subject to their making members' contributions to the Scheme on the same basis. The Company has also established an unapproved scheme to provide additional death-in-service benefits to these directors in line with their actual basic salaries.

Under the Scheme, the normal retirement age of executive directors is 60 and the basic rate of accrual is 1/50th.

Stephen Booty also receives a cash sum to enhance these benefits to an accrual rate of 1/30th.

Since the Scheme was closed to new entrants in April 2003, newly appointed employees, including executive directors, are eligible to join the Nestor Healthcare Group Personal Pension Plan ("GPP"), which is a defined contribution arrangement. In respect of executive directors, the Company makes contributions to the GPP at a rate (subject to Inland Revenue capped limits) up to a maximum of 20% of the director's basic salary. If a director is eligible to have contributions at a rate of 20% of his basic salary paid by the Company, but such payment would be in excess of the Inland Revenue capped limits, then any shortfall is instead paid to the director in cash (taxed in the normal way) as compensation in lieu of pension contributions.

Executive directors' contracts of service (non-audited)

Policy

It is the Committee's policy only to offer contracts terminable on no more than 12 months' notice to executive directors. All currently serving executive directors have contracts of employment terminable in all circumstances on a maximum of 12 months' notice. When offering contracts of employment to newly appointed executive directors, the Committee has regard to the broad principles outlined in the ABI and NAPF's joint statement on Best Practice on Executive Contracts and Severance, including the director's duty to mitigate his losses in the event of early termination of his contract.

Specific Contractual Details

Current executive directors

	Date of contract	Notice period	Termination provisions		
			"Pay in lieu of notice" clause	Share options	Annual bonus
Stephen Booty	1st February 2003	12 months' notice from Company	Note 1	Note 2	Note 3
Martyn Ellis	23rd May 2003	12 months' notice from Company	Note 1	Note 2	Note 3
William Holmes	1st October 2001	12 months' notice from Company	Note 1	Note 2	Note 3

Notes

- The Company may terminate the director's employment without notice, provided it pays to him an amount equating to his salary, benefits and employer's pension contributions or credits him with an additional period of pensionable service (as applicable) for the unexpired period of notice due under the contract. Martyn Ellis's contract permits the Company to pay any monies due on a monthly basis and, at its discretion, to cease or reduce payments if he accepts suitable alternative employment.
- At the Board's discretion, the director may be entitled to retain any vested share options held under the Group's Share Option Schemes for a period of up to 12 months from termination. He may also be entitled to exercise unvested share options early in certain specified circumstances subject to the Committee taking account of the performance of the Company and the length of time elapsed since the grant date.
- Depending on the time of year at which his employment ceases, the director may be entitled to any bonus earned by him (but not yet paid) for the previous year under the Group's bonus scheme.

Chairman and non-executive directors (non-audited)

The Board sets the fee levels for the Chairman and non-executive directors. Non-executive directors do not hold contracts of employment but are offered letters of appointment for a fixed period of three years, renewable annually thereafter by agreement. Non-executive directors do not participate in any of the Group's annual or long-term incentive arrangements, nor is their remuneration pensionable.

Current non-executive directors

	Date of letter of appointment	Appointment term	Compensation in the event of early termination of office
John Rennocks	1st October 2003	3 years from 1st October 2003	3 months' fees
Ingrid Alexander	25th July 2001	3 years from 13th August 2001 (extendable by up to 3 further periods of 12 months each)	None
Roger Dye	9th January 2004	3 years from 1st January 2004	None
Sir Andrew Foster	16th January 2004	3 years from 1st January 2004	None

Directors' emoluments (audited)

	Basic salary and fees 2005 £000	Performance related bonuses 2005 £000	Taxable benefits 2005 £000	Compensation for loss of office (including pensions) 2005 £000	Total emoluments	
	2005 £000	2005 £000	2005 £000	2005 £000	2005 £000	2004 £000
Ingrid Alexander	29	–	–	–	29	29
Stephen Booty	302	–	120	–	422	500
Roger Dye	37	–	–	–	37	33
Martyn Ellis	196	–	31	–	227	281
Sir Andrew Foster	37	–	–	–	37	33
William Holmes	160	–	18	–	178	210
John Rennocks	90	–	–	–	90	106
Justin Jewitt	–	–	–	–	–	517
Stephen Page	–	–	–	–	–	338
Total 2005	851	–	169	–	1,020	–
Total 2004	1,027	266	180	574	–	2,047

Benefits receivable consist primarily of company car provision or car allowance, car fuel and healthcare insurance.

No bonuses were earned by directors in the year.

Included in taxable benefits relating to Stephen Booty is a payment of £100,000 representing compensation in lieu of pension contribution. Included in taxable benefits relating to Martyn Ellis is a payment of £19,000 representing compensation in lieu of pension contribution.

Roger Dye and Sir Andrew Foster were appointed as directors on 19th January 2004.

Justin Jewitt resigned as a director on 27th May 2004 and Stephen Page resigned as a director on 3rd August 2004.

The figures above represent emoluments earned as directors during the relevant financial year. All are paid in the year that they are earned, with the exception of bonuses, which are paid in the year following that in which they were earned.

Directors' pensions (audited)

Defined benefit scheme

	Accrued pension per annum at 31st December 2005 £000	Increase in accrued pension during 2005 £000	Increase in accrued pension per annum during 2005 excluding price inflation £000	Transfer value of accrued pension at 31st December 2005 £000	Transfer value of accrued pension at 31st December 2004 £000	Transfer value of the increase excluding price inflation less director's contributions £000	Increase in transfer value during 2005 less director's contributions £000
Stephen Booty	14	4	4	177	115	31	47
William Holmes	13	3	3	170	117	28	45

The transfer values have been calculated on the basis of actuarial advice in accordance with the Actuarial Guidance Note GN11. The above figures exclude any benefits derived from directors' additional voluntary contributions.

Defined contribution schemes

Employer contributions of £20,940 (2004: £20,400) were paid during the year to the GPP in respect of Martyn Ellis.

Remuneration Report continued

Directors' interests (audited)

The beneficial and family interests of directors in post at the year-end in the share capital of the Company according to the register of directors' interests maintained by the Company under Section 325 of the Companies Act 1985 were:

	Ordinary Shares (non-audited)		Share Options (audited)							
			Company Plan 1996		Employee Scheme 1996		Share Option Plan 2002		SAYE Schemes	
	31.12.05	31.12.04	31.12.05	31.12.04	31.12.05	31.12.04	31.12.05	31.12.04	31.12.05	31.12.04
Ingrid Alexander	—	—	—	—	—	—	—	—	—	—
Stephen Booty	73,680 ³	57,814 ³	5,514	5,514	23,897	23,897	321,340 ⁵	124,941 ⁵	6,014	6,014
Roger Dye	—	—	—	—	—	—	—	—	—	—
Martyn Ellis	17,320 ⁴	5,262 ⁴	—	—	—	—	193,030	64,716	—	—
Sir Andrew Foster	—	—	—	—	—	—	—	—	—	—
William Holmes	4,000	4,000	5,882	5,882	43,137	43,137	175,569	70,823	13,638	10,453
John Rennocks	4,896	4,896	—	—	—	—	—	—	—	—

Notes:

- None of the directors has any non-beneficial interest in the Company's share capital.
- No director was materially interested in any contract of significance (apart from contracts of service or for services) with any Group company during or at the end of the financial year.
- Included in Stephen Booty's ordinary share holding is a total of 23,680 shares held under the LTIP (2004: 7,814).
- All of Martyn Ellis's shares are held under the LTIP.
- 112,941 options granted to Stephen Booty under the 2002 Plan in 2002 are "Super Options".
- There have been no changes in the directors' interests in the share capital between 31st December 2005 and the date of this report.

Details of share options held by the directors during the year were:

	Scheme (see below)	At 31st December 2004	Granted	Exercised	Lapsed	At 31st December 2005	Exercise price	Date from which exercisable	Expiry date
Stephen Booty	1	23,897	—	—	—	23,897	544p	Apr '05	Apr '12
	2	5,514	—	—	—	5,514	544p	Apr '05	Apr '12
	3	6,014	—	—	—	6,014	157.12p	Jun '06	Nov '06
	4	12,000	—	—	—	12,000	301p	Nov '06	Nov '13
	4	—	196,399	—	—	196,399	152.75p	Jan '08	Jan '15
Martyn Ellis	5	112,941	—	—	—	112,941	212.5p	Oct '05	Oct '12
	4	64,716	—	—	—	64,716	273.5p	Jun '06	Jun '13
William Holmes	4	—	128,314	—	—	128,314	152.75p	Jan '08	Jan '15
	1	43,137	—	—	—	43,137	510p	Oct '04	Oct '11
Justin Jewitt	2	5,882	—	—	—	5,882	510p	Oct '04	Oct '11
	3	10,453	—	—	(10,453)	—	157.12p	Jun '08	Nov '08
	3	—	13,638	—	—	13,638	121.16p	Jun '10	Nov '10
	4	58,823	—	—	—	58,823	212.5p	Oct '05	Oct '12
	4	12,000	—	—	—	12,000	301p	Nov '06	Nov '13
Stephen Page	4	—	104,746	—	—	104,746	152.75p	Jan '08	Jan '15
	1	45,883	—	—	(45,883)	—	425p	—	—
	1	22,000	—	—	(22,000)	—	542.5p	—	—
	2	7,058	—	—	(7,058)	—	425p	—	—
	4	12,000	—	—	(12,000)	—	301p	—	—
Stephen Page	1	46,561	—	—	(46,561)	—	472.5p	—	—
	2	6,349	—	—	(6,349)	—	472.5p	—	—
	3	6,014	—	—	(6,014)	—	157.12p	—	—
	4	75,294	—	—	(75,294)	—	212.5p	—	—
	4	12,000	—	—	(12,000)	—	301p	—	—
	5	75,294	—	—	(75,294)	—	212.5p	—	—

Schemes:

- Employee Share Option Scheme 1996 Options; performance target – EPS growth of RPI plus 5% per annum
- Company Share Option Plan 1996 Options; performance target – EPS growth of RPI plus 5% per annum
- SAYE Scheme Options
- The 2002 Plan – "Normal Option"
- The 2002 Plan – "Super Option"

Notes:

- 1 There is no cost to the employee for the receipt of options under the Employee Share Option Scheme 1996, Company Share Option Plan 1996 or the 2002 Plan. Deductions from earnings are made in respect of SAYE options.
- 2 Employee Share Option Scheme 1996, Company Share Option Plan 1996 and the 2002 Plan option prices are fixed at the mid-market price on the business day preceding the date of grant.
- 3 SAYE Scheme options are fixed at a discount of 20% from the average of the mid-market prices for the five business days immediately before the date of invitation.
- 4 The mid-market price at 31st December 2005 was 121.00 pence and the range during the year was 114.50 pence to 174.25 pence.
- 5 No options were exercised by directors in 2005.

On behalf of the Board



Sir Andrew Foster Chairman, Remuneration Committee
9th March 2006

Corporate Governance

Introduction

The Company complied throughout the year with the provisions set out in the Combined Code published by the UK Financial Reporting Council in July 2003 ("the Code") except where indicated in this statement.

The manner in which the Company applies the principles of good governance contained in the Code is described in the appropriate parts of this annual report. Thus the application by the Company of the Code's principles to remuneration matters at pages 19 to 25 should be read in conjunction with the statement below.

The Board

The Board of directors leads and controls the Company by holding at least eight meetings a year at which its current and forecast performance are examined. Regular reports on monthly performance and other matters of importance to the Company ensure that the Board is supplied in a timely manner with the information necessary to make an informed judgement. In addition, the Board holds regular meetings to discuss and devise the Company's medium- and long-term strategic focus and management development strategy. Regular informal presentations are given and meetings held in order to advise directors of issues of importance affecting the Group.

In accordance with the provisions of its Articles of Association and with the Code, each director is subject to re-election by the Company's shareholders at the Annual General Meeting immediately following appointment and at least every three years thereafter.

The Board has a Schedule of Matters specifically reserved to it for decision and has approved the written terms of reference for the various committees to which it has delegated its authority in certain matters. The Schedule makes it clear that all directors have access to the advice and services of the Company Secretary and establishes a procedure for all directors to take independent advice, if necessary, at the Company's expense. Matters reserved to the Board include the recommendation or approval of dividends, the approval of final and interim financial statements, major financial commitments, the acquisition of companies or businesses, appointments to the Board and its committees, the Group's future strategy and the Group's internal controls. This Schedule is kept under regular review.

During the year, the Board was led by John Rennocks, the non-executive Chairman. He also served as a member of the Board's Audit, Remuneration and Nomination Committees.

The Chairman's responsibilities are clearly defined in a written specification agreed by the Board prior to his appointment in 2003. They include the smooth running of the Board, effective communication between executive and non-executive directors and the general progress and long-term development of the Group. His other significant commitments were disclosed to the Board prior to his appointment.

The day-to-day running of the Company's business is delegated to an executive team of three executive directors led by Stephen Booty, Chief Executive and which also comprises Martyn Ellis, Finance Director and Dr William Holmes, who is responsible for the Group's clinical governance.

During the year, three independent non-executive directors with extensive business, finance, health and social care backgrounds provided the Board with a breadth of experience and with independent judgement. Ingrid Alexander, CBE, Roger Dye and Sir Andrew Foster served throughout the year, with Sir Andrew Foster being nominated as the senior independent non-executive director.

Having reviewed the Code, the Board considers that its present membership, comprising three independent non-executive directors, three executive directors and the Chairman, is appropriate, with a balance of skills and experience appropriate for the requirements of the business. This recognises that in John Rennocks, the Board has a Chairman who remains de facto "independent" (having met the criteria of independence referred to in Provision A 3.1. of the Code on his appointment in October 2003). It also considers that the Board's policies and procedures are of sufficient strength to ensure that the performance and proceedings of the Company are effectively challenged and controlled.

The Board actively encourages all directors to deepen their knowledge of their roles and responsibilities and to gain a clear understanding of the Company and the environment in which it operates. Newly appointed Board members undergo an induction programme and have received the opportunity to receive formal training. In 2005, the Group's non-executive directors received the opportunity to meet with various members of the Group's management teams on several occasions. Further training for directors is available and offered as appropriate.

In 2004, the Board adopted a formal process for reviewing its own effectiveness and that of its individual members. In addition, it formalised its previously informal policy of holding regular meetings of the non-executive directors without the executive directors, and at least once a year, without the Chairman present, in order to evaluate his performance. This process and policy have been in place throughout 2005. A formal review by the Board of its own effectiveness concluded in January 2005. This review will be repeated in 2006. Assessments of individual directors also took place during the year, culminating in a formal review that summarised and considered all results in November 2005. The assessments made by the non-executive directors of the Chairman's performance were similarly summarised and formally reviewed at the same time.

All non-executive directors meet the criteria of independence as laid down in Provision A 3.1. of the Revised Code with the exception of John Rennocks who met all of the criteria of independence on appointment and whom the Board currently regards de facto independent. For this reason, he remains a member of each of the Board's Nomination, Remuneration and Audit Committees. However, it intends to keep this under review.

Committees

The Board operates three committees, consisting wholly of non-executive directors to which it has delegated certain specific responsibilities and each of which has formally adopted terms of reference. These comprise the Nomination, Audit and Remuneration Committees.

Nomination Committee

The Nomination Committee, which makes recommendations to the Board on the appointment of directors, is chaired by John Rennocks. The Committee draws on the advice of the Group's Director of Human Resources and such professional advisors as it considers necessary.

The Committee comprises John Rennocks, Ingrid Alexander, Roger Dye and Sir Andrew Foster.

The terms of reference of the Nomination Committee are regularly reviewed by the Board.

No changes to the composition of the Board were made or contemplated during the year, so no meetings of the Nomination Committee were in practice required.

Audit Committee

The Audit Committee is chaired by Roger Dye, a chartered accountant and Chief Executive of the Davis Service Group Plc. It comprises only non-executive directors but includes John Rennocks as the Board is of the opinion that the Committee's work benefits from his financial expertise and experience gained as a former executive finance director and as Chairman of the Audit Committee of a number of other publicly listed companies.

The other members of the Committee comprise Ingrid Alexander and Sir Andrew Foster and its terms of reference are regularly reviewed by the Board.

The Committee met three times during the year to review the preliminary and interim results before they were presented to the Board, to receive reports from the Company's external auditors, to receive reports from the Company's Business Review Team (responsible for carrying out the internal audit function and accountable to the Audit Committee) and to make recommendations to the Board on accounting policies. Its primary duties include the monitoring, on behalf of the Board, of compliance with and the effectiveness of the Company's accounting and internal control systems. The Committee's duties also include monitoring the scope and results of the Company's annual audit and the independence, general performance and objectivity of its auditors. The Committee has also agreed and implemented a procedure for reviewing and assessing its own effectiveness, which culminated in a formal review and communication of summary results to the Board in November 2005. From time to time the Chairman of the Committee also meets informally with the auditors.

Remuneration Committee

The Remuneration Committee's responsibilities include determining the Group's overall remuneration strategy and the remuneration packages of the executive directors and other senior executives, after having consulted with the Chief Executive and having received professional advice from remuneration consultants and the Group's Director of Human Resources. The Committee is also responsible for approving the grant and exercise of executive long-term incentive arrangements. In determining remuneration policy, the Committee is free to obtain such professional advice as it sees fit, and regularly monitors both the policies of comparator companies and current market practice, in order to ensure that the packages provided are sufficient to attract and retain executive directors of the necessary quality.

The remuneration of non-executive directors, including the Chairman, is a matter for the Company's Board and the Committee's terms of reference make it clear that the framework for the remuneration of the Company's senior executives (including executive directors) must be agreed by the Board as a whole.

The terms of reference of the Committee are regularly reviewed by the Board.

The Committee met three times in the year.

Sir Andrew Foster acted as Chairman of the Remuneration Committee throughout the year. The other members of the Committee are Ingrid Alexander, Roger Dye and John Rennocks, who is currently considered by the Board to be "de facto" independent and whose membership is therefore appropriate, although this is subject to ongoing review.

Short biographies of each of the directors, including their membership of the Board's committees outlined above, may be found on pages 14 and 15.

Corporate Governance continued

Attendance at Meetings

All directors attended those Board and Committee meetings to which they were entitled to attend, with just one exception: Sir Andrew Foster was unable to attend one meeting of the Audit Committee.

The Board, on the Company's behalf, recognises the need to maintain an active dialogue with its shareholders. The Chief Executive and Finance Director meet regularly with institutional investors and analysts to discuss the Company's performance and all shareholders have access to the senior non-executive director, who is available to discuss any questions which investors may have in relation to the running of the Company. They also have access to the Chairman of the Company if they so require, although in 2005 only one such meeting took place. The Board encourages shareholders to attend the Annual General Meeting and is always willing to answer questions, either in the meeting itself or, more informally, afterwards. In addition, shareholders may contact the Company direct, either through its website or by telephoning its offices on 01784 221600.

The Board also recognises the need to ensure that all directors are fully aware of the views of major shareholders about the Company. Copies of all analysts' research relating to the Company are circulated to all directors upon publication, quarterly analyses of the Company's shareholder register are made available to the Board and written feedback from shareholders and analysts, prepared by the Company's brokers and public relations advisors, is provided to all directors after every significant corporate event and at least twice a year.

Going Concern

The directors confirm that, after reviewing the financial position and cash flows of the Group and of the Company, they have a reasonable expectation that the Group and the Company have adequate resources to continue in operational existence for the foreseeable future. For this reason, they continue to adopt the going concern basis in preparing the accounts.

Internal Controls

As required by the UK Listing Authority, the Company has complied throughout the year with the provisions of the Code relating to internal controls, having implemented the procedures necessary to comply with the guidance issued in September 1999 (the Turnbull Committee Report) and to report in line with that guidance.

The Board is responsible for the Group's system of internal control and for reviewing its effectiveness. Such a system is designed to manage rather than eliminate the risk of failure to achieve business objectives and can only provide reasonable and not absolute assurance against material misstatement or loss.

The directors first adopted a revised comprehensive process for managing, evaluating and reporting on significant risks faced by the Group in 1999. This process has been constantly reviewed and revised in subsequent years, including 2005. The revised (and further refined and extended) process has been in place for the whole of 2005 and up to the date of approval of the Annual Report and Accounts.

The key elements of the system operated by the Group to identify, evaluate and manage significant risks include the following:

- The Group's management operates a formal process for identifying, managing and reporting on operational, clinical and financial risks faced by each of the Group's businesses, whereby each of the risks identified is reviewed in detail by the executive directors on a semi-annual basis. Senior management team review meetings are held on at least a monthly basis at which the Group's business managers and executive team members report on the progress of the companies or discipline for which they are responsible and share best practice. The formal process for identifying discipline-specific risks across the Group's operations encompasses financial, IT, human resources, legal, property and clinical risks. A mechanism also exists to extend the Group's formal risk management processes to any significant new business acquired or begun by the Company immediately upon acquisition or start-up. In this way, the Board is able to confirm that the necessary process has been operated by the Group for the whole of 2005.
- At least twice a year, the Audit Committee of the Board reviews a register compiled by the managing director of each of the Group's businesses and registers compiled by certain members of the Group's senior management team, summarising the significant risks faced by the businesses or the Group as a whole, the likelihood of those risks occurring and the steps being taken to minimise or otherwise manage those risks.
- In 2004, the Board took steps better to align its risk management processes with the operational imperatives of the businesses by adopting a dynamic risk-management process that assists the Group's operational management to identify developing trends at an early stage. This has been used throughout 2005.

As required by the Turnbull Guidance, the Board has carried out an annual assessment of the effectiveness of the system of internal controls. The processes applied by the Board include:

- At the end of the year, the managing directors of each of the Group's businesses, including the Group's corporate resource, are required to complete and sign a register of the key financial and operational risks facing the business for which they are responsible and to confirm that they have complied throughout the year with the Company's policies and procedures on risk management. From these registers, a report identifying the key risks faced by the Group is compiled and signed by the Chief Executive, Finance Director and Company Secretary, who are also required to confirm their compliance with such procedures and policies. This report and the annual compliance statements of each of the managing directors are reviewed by the Board before the Annual Report and Accounts are approved.
- The Group has an independent Internal Audit function, carried out by its Business Review Team, which reviews the overall effectiveness of the risk management process for the key risks and reports independently to the Audit Committee.
- At each meeting the Audit Committee reviews reports of the senior management team, internal and external auditors, on any issues identified as having a potentially substantial impact on the results of the Group, or areas of control weakness.
- The Audit Committee reviews the effectiveness of the Group's system of managing financial risk and refers any risks it considers significant to the Board for its consideration.
- At least twice a year, the Audit Committee reviews the work plans and results of each of the internal and external auditors.
- The Audit Committee Chairman reports the outcome of all Audit Committee meetings to the Board, which also receives minutes of all such meetings.

Auditors' Report

Report to the shareholders of Nestor Healthcare Group plc

Independent auditors' report to the members of Nestor Healthcare Group plc

We have audited the Group and Company financial statements (the "financial statements") of Nestor Healthcare Group plc for the year ended 31st December 2005 which comprise the Group Income Statement, the Group and Company Balance Sheets, the Group Statement of Recognised Income and Expense, the Group and Company Cash Flow Statements, and the related notes. These financial statements have been prepared under the accounting policies set out therein. We have also audited the information in the Directors' Remuneration Report that is described as having been audited.

Respective responsibilities of directors and auditors

The directors' responsibilities for preparing the Annual Report, the Directors' Remuneration Report and the financial statements in accordance with applicable law and International Financial Reporting Standards (IFRS) as adopted by the European Union are set out in the Statement of Directors' Responsibilities.

Our responsibility is to audit the financial statements and the part of the Directors' Remuneration Report to be audited in accordance with relevant legal and regulatory requirements and International Standards on Auditing (UK and Ireland). This report, including the opinion, has been prepared for and only for the Company's members as a body in accordance with Section 235 of the Companies Act 1985 and for no other purpose. We do not, in giving this opinion, accept or assume responsibility for any other purpose or to any other person to whom this report is shown or into whose hands it may come save where expressly agreed by our prior consent in writing.

We report to you our opinion as to whether the financial statements give a true and fair view and whether the financial statements and the part of the Directors' Remuneration Report to be audited have been properly prepared in accordance with the Companies Act 1985 and Article 4 of the IAS Regulation. We also report to you if, in our opinion, the Directors' Report is not consistent with the financial statements, if the Company has not kept proper accounting records, if we have not received all the information and explanations we require for our audit, or if information specified by law regarding directors' remuneration and other transactions is not disclosed.

We review whether the Corporate Governance Statement reflects the Company's compliance with the nine provisions of the 2003 FRC Combined Code specified for our review by the Listing Rules of the Financial Services Authority, and we report if it does not. We are not required to consider whether the board's statements on internal control cover all risks and controls, or form an opinion on the effectiveness of the Group's corporate governance procedures or its risk and control procedures.

We read other information contained in the Annual Report and consider whether it is consistent with the audited financial statements. The other information comprises only the Chairman's Statement, the Chief Executive's Review, the Financial Review, the Clinical Governance Statement, the Employees and Social Responsibility Statement, the Directors' Report, the unaudited part of the Directors' Remuneration Report and the Corporate Governance Statement. We consider the implications for our report if we become aware of any apparent misstatements or material inconsistencies with the financial statements. Our responsibilities do not extend to any other information.

Basis of audit opinion

We conducted our audit in accordance with International Standards on Auditing (UK and Ireland) issued by the Auditing Practices Board. An audit includes examination, on a test basis, of evidence relevant to the amounts and disclosures in the financial statements and the part of the Directors' Remuneration Report to be audited. It also includes an assessment of the significant estimates and judgements made by the directors in the preparation of the financial statements, and of whether the accounting policies are appropriate to the Group's and Company's circumstances, consistently applied and adequately disclosed.

We planned and performed our audit so as to obtain all the information and explanations which we considered necessary in order to provide us with sufficient evidence to give reasonable assurance that the financial statements and the part of the Directors' Remuneration Report to be audited are free from material misstatement, whether caused by fraud or other irregularity or error. In forming our opinion we also evaluated the overall adequacy of the presentation of information in the financial statements and the part of the Directors' Remuneration Report to be audited.

Opinion

In our opinion:

- the Group financial statements give a true and fair view, in accordance with IFRS as adopted by the European Union, of the state of the Group's affairs as at 31st December 2005 and of its profit and cash flows for the year then ended;
- the Company financial statements give a true and fair view, in accordance with IFRS as adopted by the European Union as applied in accordance with the provisions of the Companies Act 1985, of the state of the Company's affairs as at 31st December 2005 and cash flows for the year then ended; and
- the financial statements and the part of the Directors' Remuneration Report to be audited have been properly prepared in accordance with the Companies Act 1985 and Article 4 of the IAS Regulation.

PricewaterhouseCoopers LLP
PricewaterhouseCoopers LLP

Chartered Accountants and Registered Auditors
London
9th March 2006

Group Income Statement

for the year ended 31st December 2005

	Notes	2005 £000	2004 £000
Revenue	3	309,035	389,839
Cost of sales		(226,891)	(291,361)
Gross profit		82,144	98,478
Administrative expenses		(62,253)	(140,398)
Analysed as:			
Administrative expenses excluding goodwill impairment		(62,253)	(91,289)
Goodwill impairment	4	–	(49,109)
Operating profit/(loss)	3	19,891	(41,920)
Analysed as:			
Operating profit before goodwill impairment		19,891	7,189
Goodwill impairment	4	–	(49,109)
Finance income	5	30	64
Finance expense	5	(5,672)	(5,672)
Profit/(loss) before taxation		14,249	(47,528)
Tax expense	6	(3,795)	(2,364)
Profit/(loss) for the year		10,454	(49,892)
Profit attributable to minority interests	24	203	118
Profit/(loss) attributable to equity shareholders		10,251	(50,010)
Profit/(loss) for the year		10,454	(49,892)
Earnings/(loss) per 10p share			
Basic	9	11.70p	(57.07p)
Diluted	9	11.69p	(57.07p)
Equity dividends	8	(2,190)	(5,381)
Dividends per share	8	2.50p	6.14p

Group and Company Balance Sheets

as at 31st December 2005

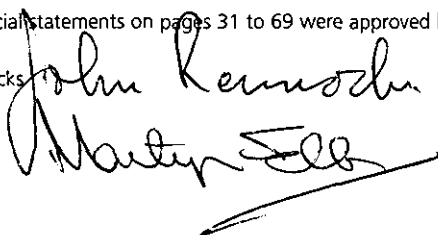
		Group		Company	
	Notes	2005 £000	2004 £000	2005 £000	2004 £000
Non-current assets					
Goodwill	10	113,839	114,199	-	-
Other intangible assets	10	739	641	-	-
Property, plant and equipment	11	5,105	7,534	-	23
Deferred tax assets	14	7,336	6,629	-	-
Investments	13	-	-	114,123	113,698
Non-current assets		127,019	129,003	114,123	113,721
Current assets					
Trade and other receivables	15	39,632	50,928	112,614	127,313
Cash and cash equivalents	19	2,098	979	-	114
Current assets		41,730	51,907	112,614	127,427
Current liabilities					
Financial liabilities:					
Borrowings – overdrafts	18	(987)	(1,601)	-	(7,116)
Borrowings – loans	18	(81,000)	-	(81,000)	-
Trade and other payables	16	(25,647)	(40,028)	-	(23,498)
Current tax liabilities	16	(2,012)	(2,216)	-	-
Provisions	20	(2,164)	(2,112)	-	(15)
Current liabilities		(111,810)	(45,957)	(81,000)	(30,629)
Net current (liabilities)/assets		(70,080)	5,950	31,614	96,798
Total assets less current liabilities		56,939	134,953	145,737	210,519
Non-current liabilities					
Financial liabilities:					
Borrowings – loans	18	-	(84,000)	-	(84,000)
Other payables		-	(1)	-	-
Provisions	20	(17,764)	(19,728)	-	(371)
Non-current liabilities		(17,764)	(103,729)	-	(84,371)
Net assets		39,175	31,224	145,737	126,148
Equity					
Called up share capital	21	8,763	8,763	8,763	8,763
Share premium account	22	43,224	43,224	43,224	43,224
Share payment reserve	22	636	211	636	211
Other reserves	22	864	864	25,750	25,750
Retained (losses)/earnings	22	(14,565)	(21,888)	67,364	48,200
Equity shareholders' funds		38,922	31,174	145,737	126,148
Minority interests in equity	24	253	50	-	-
Total equity		39,175	31,224	145,737	126,148

The notes on pages 34 to 69 form an integral part of these financial statements.

The financial statements on pages 31 to 69 were approved by the Board on 9th March 2006 and were signed on its behalf by:

J L Rennocks

M A Ellis



Group Statement of Recognised Income and Expense

for the year ended 31st December 2005

	Notes	2005 £000	2004 £000
Profit/(loss) for the year		10,454	(49,892)
Actuarial losses arising in defined benefit pension schemes	30	(1,054)	(148)
Deferred taxation arising on actuarial losses		316	44
Net recognised income/(expense)	23	9,716	(49,996)

Net recognised income/(expense) for the Company was the same as its profit/(loss) in both 2005 and 2004 (see note 7).

Group and Company Cash Flow Statements

for the year ended 31st December 2005

	Group		Company	
	2005 £000	2004 £000	2005 £000	2004 £000
Operating activities				
Cash generated from operations (note 25)	20,956	26,692	17,128	142,881
Interest paid	(5,556)	(5,620)	(4,959)	(5,151)
Interest received	30	64	–	64
Income taxes paid	(4,390)	(3,930)	–	–
Net cash generated from operating activities	11,040	17,206	12,169	137,794
Investing activities				
Purchase of property, plant and equipment (note 11)	(632)	(2,823)	–	(4)
Sale of property, plant and equipment	250	280	23	–
Purchase of businesses and subsidiary undertakings (note 13)	(3,735)	(4,930)	–	(113,487)
Net cash acquired with subsidiary undertakings	–	368	–	–
Net cash (used in)/generated from investing activities	(4,117)	(7,105)	23	(113,491)
Financing activities				
Issue of ordinary share capital	–	2	–	2
Capital element of finance lease payments	–	(14)	–	–
Equity dividends paid to shareholders (note 8)	(2,190)	(5,381)	(2,190)	(5,381)
Decrease in loans from banks	(3,000)	(6,000)	(3,000)	(6,000)
Decrease in loans other than from banks	–	(1,407)	–	(1,407)
(Decrease)/increase in bank overdrafts	(614)	750	(7,116)	(12,721)
Net cash used in financing activities	(5,804)	(12,050)	(12,306)	(25,507)
Net increase/(decrease) in cash and cash equivalents	1,119	(1,949)	(114)	(1,204)
Cash and cash equivalents at beginning of the year	979	2,928	114	1,318
Net increase/(decrease) in cash and cash equivalents	1,119	(1,949)	(114)	(1,204)
Cash and cash equivalents at end of the year	2,098	979	–	114

Notes to the Financial Statements

for the year ended 31st December 2005

1 Basis of preparation

The financial information presented in this document has been prepared in accordance with International Financial Reporting Standards (IFRS) as endorsed by the European Union and International Financial Reporting Interpretations Committee (IFRIC) interpretations and with those parts of the Companies Act, 1985 applicable to companies reporting under IFRS that are applicable to the consolidated financial statements for the year ending 31st December 2005.

These financial statements have been prepared under the historical cost convention.

A summary of the significant accounting policies used in the preparation of these financial statements under IFRS is provided in note 2 below.

IFRS 1, First time adoption of International Financial Reporting Standards, sets out the requirements for companies preparing financial statements under IFRS for the first time and requires the accounting policies to be applied retrospectively. IFRS 1 contains the option to take advantage of certain exemptions to the retrospective application. The Group has applied such optional exemptions as follows:

- The provisions of IFRS 3 – Business combinations have been applied to acquisitions made since 1st January 2004
- The provisions of IFRS 2 – Share-based payments have been applied only to awards made after 7th November 2002
- The accumulated actuarial gains and losses in relation to employee defined benefit pension schemes have been recognised in full at 1st January 2004 and all subsequent movements in the actuarial valuations have been taken through the statement of recognised income and expense

Estimates and judgements

The preparation of accounts in accordance with IFRS requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the accounts and the reported amounts of revenues and expenses during the reported period. These estimates are based on historical experience and various other assumptions that management and directors believe are reasonable under the circumstances, the results of which form the basis for making judgements about the carrying value of assets and liabilities that are not readily apparent from other sources.

Areas comprising critical judgements that may significantly affect the Group's earnings and financial position are revenue collection, valuation of intangibles including goodwill, restructuring activities, provisions for pensions, income taxes, property related items and share-based payments, all of which are discussed in the respective notes.

2 Accounting policies

Basis of consolidation

The accounting reference date of the Group, comprising the Company and all its trading subsidiary undertakings, is 31st December. These financial statements are accordingly presented for the year to 31st December 2005.

The results of businesses acquired are included from the effective date of acquisition and businesses sold are included up to the effective date of disposal. The effective date of acquisition or disposal is considered to be the date when control passes. Acquisitions have been accounted for using the purchase method of accounting. The cost of acquisition so accounted for includes directly related capitalised costs.

Revenue

Revenue is recognised in the income statement when goods or services are supplied to external customers against orders received.

Goodwill

Where the cost of acquisition exceeds the fair values attributable to the net assets acquired, the resulting goodwill is capitalised. Goodwill is tested for impairment annually and also when indicators suggest that the carrying value may not be recoverable. Goodwill is carried at cost less amortisation charged prior to the Group's transition to IFRS on 1st January 2004 less accumulated impairment losses. Any impairment is recognised in the period in which it is identified.

Prior to the adoption of IFRS, goodwill was amortised over a period not exceeding 20 years. Prior to 1st January 1998, all purchased goodwill was written off to reserves on acquisition. Under IFRS 1, such goodwill is not recognised on transition to IFRS nor is the goodwill transferred to the income statement on disposal of the investment or if the investment becomes impaired.

Other intangible assets

Other intangible assets chiefly represent the capitalised value of customer contracts. Such contracts are capitalised at cost (or at fair value if acquired through a business combination) and amortised over a period equal to the remaining life of each contract. The carrying value is reviewed for impairment if events or changes in circumstances indicate the carrying value may not be recoverable.

Property, plant and equipment

Tangible fixed assets are stated at cost less depreciation and impairment. Depreciation is calculated so as to write down the cost of tangible assets to their estimated residual value in equal instalments over their estimated useful lives. The ranges of estimated useful lives for each major asset category, which are reviewed annually, are:

Leasehold land and buildings	Term of the lease
Plant and equipment, fixtures and fittings (including computer equipment)	3 to 8 years

The carrying value is reviewed for impairment if events or changes in circumstances indicate the carrying value may not be recoverable.

Investments

Investments in subsidiary undertakings are held at original cost less any provision for impairment.

Leases

Leasing agreements which transfer to the Group substantially all the risks and benefits incidental to ownership of the fixed asset being leased are finance leases. Assets held under finance leases are recognised as assets of the Group at their fair value, or, if lower, at the present value of the minimum lease payments, each determined at the inception of the lease. The corresponding lease commitments are treated as obligations to the lessor. Lease payments are apportioned between finance charges and reduction of the lease obligations so as to achieve a constant rate of interest on the remaining balance of the liability. Payments under all other lease arrangements, known as operating leases, are charged to the income statement in the period to which they relate.

Corporation tax

The amount included in the income statement is based on pre-tax reported profit or loss and is calculated at current tax rates, taking into account temporary differences and the likelihood of realisation of deferred tax assets and liabilities.

Deferred taxation

Deferred tax is provided in full, using the liability method, on temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the financial statements. Deferred tax assets are recognised to the extent that it is probable that future taxable profits will be available against which the temporary differences can be utilised.

Deferred tax is provided using rates of tax that have been enacted or substantively enacted by the balance sheet date. Deferred tax assets and liabilities are not discounted.

Employee benefits

The costs of providing pensions under defined benefit schemes are calculated using the projected unit credit method and spread over the period during which benefit is expected to be derived from the employee's services, in accordance with the advice of qualified actuaries. Pension obligations are measured at the present value of estimated future cash flows discounted at rates reflecting the yields of high quality corporate bonds. Pension scheme assets are measured at fair value at the balance sheet date. Actuarial gains and losses, differences between the expected and actual returns, and the effects of changes in actuarial assumptions are recognised in the statement of recognised income and expense in the year they arise.

The Group's contributions to defined contribution schemes are charged to the income statement as incurred.

Share-based payments

IFRS 2 has been applied to all grants of equity instruments after 7th November 2002 in accordance with the transitional provisions of the standard. The Group issues equity-settled share-based payments to certain employees under the terms of various employee share and share option schemes, including long-term incentive plans and Save As You Earn share option schemes. Equity-settled share-based payments are measured at fair value at the date of grant. The fair value so determined at the grant date is expensed on a straight line basis over the vesting period, based on an estimate of the shares that will ultimately vest. Fair value has been measured using a stochastic simulation modelling valuation method.

The fair values of awards granted prior to 7th November 2002 have not been charged to income.

Provisions

Provisions are made when an obligation exists for a future liability in respect of a past event and where the amount of the obligation can be reliably estimated. If the effect of the time value of money is material, provisions are determined by discounting the expected future cash flows at a pre-tax rate that reflects current market assessments of the time value of money and, where appropriate, the risks specific to the liability. Where discounting is used, the increase in the provision due to the passage of time is recognised as a finance expense.

Foreign currency

Assets and liabilities denominated in foreign currencies are translated into sterling at the period end exchange rates.

Notes to the Financial Statements

for the year ended 31st December 2005

3 Segmental reporting

Operations are conducted and managed through three segments – Healthcare Staffing, Social Care and Primary Care, with segmental results reported on this basis. Costs have been allocated on a specific basis where possible, and certain central costs allocated on a reasonable and consistent basis.

In 2005 the results of certain businesses have been reclassified between business segments. The segmental analyses of revenue, operating profit/(loss) and operating assets below reflect this revised business reclassification.

The UK was the origin and destination of all of the Group's revenue in both 2005 and 2004. All revenue is derived from external customers. Materially all of the Group's operating profits/(losses) were earned in the UK, and materially all of the Group's operating assets and net assets were located in the UK, in both 2005 and 2004.

	2005 £000	2004 £000
Revenue by business segment		
Healthcare Staffing	113,109	155,120
Social Care	108,759	111,954
Primary Care	87,167	122,765
Total	309,035	389,839
	Operating profit/(loss) before goodwill impairment	
	2005 £000	2004 £000
Operating profit/(loss) by business segment before goodwill impairment		
Healthcare Staffing	4,329	1,653
Social Care	12,645	7,830
Primary Care	2,917	(2,294)
Total operating profit/(loss) by business segment before goodwill impairment	19,891	7,189
	Profit/(loss) after goodwill impairment	
	2005 £000	2004 £000
Profit/(loss) for the year		
Operating profit/(loss) by business segment after goodwill impairment:		
Healthcare Staffing	4,329	1,653
Social Care	12,645	7,334
Primary Care	2,917	(50,907)
Total operating profit/(loss) by business segment after goodwill impairment	19,891	(41,920)
Finance income	30	64
Finance expense	(5,672)	(5,672)
Profit/(loss) before taxation	14,249	(47,528)
Tax expense	(3,795)	(2,364)
Profit/(loss) for the year	10,454	(49,892)

Central costs have been allocated across the business segments on the basis of activity and on a consistent and reasonable basis.

3 Segmental reporting continued

Revenue, cost of sales, gross profit, administrative expenses and operating profit/(loss) are analysed between existing and acquired operations as follows:

	Continuing – existing 2005 £000	Continuing – acquisitions 2005 £000	Total 2005 £000	Total 2004 £000
Revenue	306,332	2,703	309,035	389,839
Cost of sales	(225,115)	(1,776)	(226,891)	(291,361)
Gross profit	81,217	927	82,144	98,478
Total administrative expenses	(61,750)	(503)	(62,253)	(140,398)
Operating profit/(loss)	19,467	424	19,891	(41,920)

The contribution from acquisitions shown above reflects the contribution from businesses that were acquired during the year. In 2005 the one business acquired is reported within the Social Care business segment.

	Segment assets 2005 £000	Segment liabilities 2005 £000	Net operating assets 2005 £000
Analysis of operating assets and liabilities by business segment – 2005			
Healthcare Staffing	48,605	(13,980)	34,625
Social Care	57,343	(8,466)	48,877
Primary Care	56,708	(13,159)	43,549
Central	3,995	(11,982)	(7,987)
Total operating assets/(liabilities), including goodwill, at 31st December 2005	166,651	(47,587)	119,064

	2005 £000
Net assets per Group balance sheet	39,175
Net debt	79,889
Total net operating assets, including goodwill, at 31st December 2005	119,064

	Segment assets 2004 £000	Segment liabilities 2004 £000	Net operating assets 2004 £000
Analysis of operating assets and liabilities by business segment – 2004			
Healthcare Staffing	56,273	(17,103)	39,170
Social Care	56,911	(19,960)	36,951
Primary Care	57,559	(21,314)	36,245
Central	9,188	(5,708)	3,480
Total operating assets/(liabilities), including goodwill, at 31st December 2004	179,931	(64,085)	115,846

	2004 £000
Net assets per Group balance sheet	31,224
Net debt	84,622
Total net operating assets, including goodwill, at 31st December 2004	115,846

Notes to the Financial Statements

for the year ended 31st December 2005

3 Segmental reporting continued

	Capital expenditure	Acquisitions	Depreciation	Amortisation of intangibles	Impairment of goodwill
	2005	2005	2005	2005	2005
	£000	£000	£000	£000	£000
Analysis of other segment items – 2005					
Healthcare Staffing	56	–	245	–	–
Social Care	187	1,854	976	344	–
Primary Care	143	–	1,243	–	–
Central	246	–	351	–	–
Total	632	1,854	2,815	344	–

	Capital expenditure	Acquisitions	Depreciation	Amortisation of intangibles	Impairment of goodwill
	2004	2004	2004	2004	2004
	£000	£000	£000	£000	£000
Analysis of other segment items – 2004					
Healthcare Staffing	478	–	1,402	–	–
Social Care	885	3,097	450	272	496
Primary Care	1,298	–	2,297	–	48,613
Central	162	–	487	–	–
Total	2,823	3,097	4,636	272	49,109

4 Operating profit/(loss)

	Group		Company	
	2005	2004	2005	2004
	£000	£000	£000	£000
Operating profit/(loss) is stated after charging/(crediting):				
Employee costs	111,982	130,163	–	–
Impairment of goodwill	–	49,109	–	–
Amortisation of intangible assets	344	272	–	–
Depreciation of property, plant and equipment	2,815	4,636	–	39
Profit on sale of property, plant and equipment	(4)	(128)	–	–
Share-based payments charge	425	162	–	–
Auditors' remuneration – statutory audit	270	387	–	–
Operating lease rentals:				
Land and buildings	3,589	4,732	–	–
Plant and machinery	550	1,482	–	–
Significant costs relating to a fundamental restructuring:				
Asset impairments and write offs	–	4,844	–	–
Onerous property lease costs	–	4,903	–	–
Severance and other reorganisation costs	–	2,084	–	1,203
Settlement of tax liability relating to a discontinued operation	–	1,577	–	1,577

Remuneration of the Company's auditors in respect of other services was as shown below:

	Group	
	2005	2004
	£000	£000
Tax compliance and advisory services	222	224
Further assurance services	–	50
Structuring services	–	28
Total	222	302

Auditors' remuneration relating to the statutory audit of the Company of £25,000 (2004: £40,000) was borne by another Group company.

The impairment of goodwill accounted for in 2004 related primarily to the carrying value of goodwill arising from the purchase of the Healthcare group of companies in 2001, which was reduced by £48,613,000 at 31st December 2004 following a reforecasting exercise. In addition, the carrying value of goodwill relating to two acquisitions made in 2003 was impaired by £496,000 also at 31st December 2004. The valuation exercise assumed a long-term real growth rate of 2.25% and a nominal discount rate of 13.4% (then equivalent to the Group's weighted average cost of capital) with cash flows projected in perpetuity.

5 Finance income and expense

	2005 £000	2004 £000
Finance income		
Bank interest receivable	30	64
Total finance income	30	64
	2005 £000	2004 £000
Finance expense		
Unwinding of discount in property provisions	(229)	(115)
Interest payable on bank loans and overdrafts	(5,043)	(5,085)
Interest payable on other loans	(41)	(27)
Net interest cost of defined benefit pension schemes	(325)	(412)
Other interest payable	(34)	(33)
Total finance expense	(5,672)	(5,672)

6 Taxation

	2005 £000	2004 £000
UK corporation tax on taxable profit/(loss) for the year	(4,614)	(2,479)
Over provision in previous years – current tax	428	103
Current tax charge	(4,186)	(2,376)
Deferred tax credit for the year	331	12
Over provision in previous years – deferred tax	60	–
Deferred tax credit	391	12
Tax expense for the year	(3,795)	(2,364)

The effective tax rate for the year is lower than the standard rate (30% (2004:30%)) of corporation tax for the UK. The differences are explained below:

	2005 £000	2004 £000
Profit/(loss) at the standard rate of corporation tax at 30%	(4,275)	14,258
Non deductible exceptional charges	–	(16,436)
Other items not deductible	(94)	(123)
Goodwill impairment not deductible	–	(148)
Timing differences	86	(18)
Over provision in previous years	488	103
Tax expense for the year	(3,795)	(2,364)

7 Profit/(loss) for the year

The profit after tax for the year dealt with in the accounts of the Company amounts to £21,354,000 (2004: loss of £12,777,000). As allowed by the provisions of Section 230 of the Companies Act 1985, the Company has not published its own income statement.

8 Dividends

	2005 £000	2004 £000
Equity dividends paid		
Ordinary shares: final dividend for the previous year: 1.50p per 10p share (2004 – 6.14p)	1,314	5,381
Ordinary shares: interim dividend for the current year: 1.00p per 10p share (2004 – nil)	876	–
Total dividends: 2.50p per 10p share (2004 – 6.14p per 10p share)	2,190	5,381

In addition, the directors propose a final dividend for the year ending 31st December 2005 of 2.00p per 10p share (cost £1,753,000) and a resolution to this effect will be tabled at the Annual General Meeting. It is proposed that the dividend will be paid on 2nd June 2006 to shareholders who are on the register of members on 5th May 2006.

Notes to the Financial Statements

for the year ended 31st December 2005

9 Earnings per share

Basic earnings/(loss) per 10p share is calculated by dividing the earnings attributable to ordinary shareholders by the weighted average number of ordinary shares in issue during the year.

For diluted earnings per share, the weighted average number of ordinary shares in issue is adjusted to assume conversion of all potentially dilutive ordinary shares. The Group has only one category of potentially dilutive ordinary shares: those share options granted to employees where the exercise price is less than the average market price of the Company's ordinary shares during the year. In the year to 31st December 2005 the only such options were the 515,121 SAYE share options granted in April 2005 and the 91,703 options granted under the Share Option Plan 2002 in November 2005.

Reconciliations of the earnings and weighted average number of shares used in the calculations are set out below:

	2005 Earnings £000	2005 Weighted average number of 10p shares thousand	2005 Earnings per share pence	2004 Earnings £000	2004 Weighted average number of 10p shares thousand	2004 Earnings per share pence
Earnings/(loss) per share	10,251	87,633	11.70p	(50,010)	87,633	(57.07p)
Dilutive effect of options	-	88	(0.01p)	-	-	-
Diluted earnings/(loss) per share	10,251	87,721	11.69p	(50,010)	87,633	(57.07p)

A total of 2,891,260 share options outstanding at the end of the year were not potentially dilutive in the year to 31st December 2005.

10 Intangible assets

	2005 £000
Goodwill	
Group – 2005	
Cost	
At 1st January 2005	187,650
Additions	1,503
Reductions	(1,863)
At 31st December 2005	187,290
 Aggregate amortisation	
At 1st January 2005	73,451
Impairments	-
At 31st December 2005	73,451
 Net book value	
At 31st December 2005	113,839
	2004 £000
Group – 2004	
Cost	
At 1st January 2004	185,427
Additions	2,575
Reductions	(352)
At 31st December 2004	187,650
 Aggregate amortisation	
At 1st January 2004	24,342
Impairments	49,109
At 31st December 2004	73,451
 Net book value	
At 31st December 2004	114,199

Group goodwill derives from the acquisition of businesses and subsidiary undertakings in 2005 and prior years. In 2005, the directors have specifically evaluated the carrying values of goodwill for each such acquisition. Following conclusion of these evaluations, the directors have concluded that no impairment of goodwill is required.

10 Intangible assets continued

The carrying amounts of goodwill by business segment are as follows:

	2005 £000	2004 £000
Goodwill by business segment		
Healthcare Staffing	33,014	33,745
Social Care	39,217	38,846
Primary Care	41,608	41,608
Total	113,839	114,199

Other intangible assets	2005 £000
Group – 2005	
Cost	
At 1st January 2005	913
Additions	442
At 31st December 2005	1,355
Aggregate amortisation	
At 1st January 2005	272
Charge for the year	344
At 31st December 2005	616
Net book value	
At 31st December 2005	739

	2004 £000
Group – 2004	
Cost	
At 1st January 2004	–
Additions	913
At 31st December 2004	913
Aggregate amortisation	
At 1st January 2004	–
Charge for the year	272
At 31st December 2004	272
Net book value	
At 31st December 2004	641

Other intangible assets represent the capitalised value of customer contracts acquired via business combinations (acquisitions of businesses and subsidiary undertakings) made since 1st January 2004. Such contracts are capitalised at fair value and amortised over a period equal to the remaining life of each contract. Contract lives so amortised varied between one year and five years. All were within the Social Care business segment at both 31st December 2005 and 31st December 2004.

All of the other intangible assets were owned by subsidiary undertakings of the Company at both 31st December 2005 and 31st December 2004.

The Group carries out reviews of its intangible assets on an annual basis to determine whether events or changes in circumstances indicate that the carrying amount of the assets may not be recoverable. If any such indication exists, the recoverable amount of the asset is estimated as either the higher of the net selling price or value in use; the resultant loss (the difference between the carrying amount and the recoverable amount) is recorded as a charge to the consolidated income statement. The value in use is calculated as the present value of the estimated future cash flows expected to result from the use of assets in the business being evaluated. In order to determine the present value of estimated future cash flows, the Group uses a discount rate based on its estimated weighted cost of capital, together with any risk premium as appropriate. Estimated future cash flows used in the impairment calculations represent management's best view of likely market conditions including selling prices, volumes and employment costs. Actual cash flows may differ significantly from these estimates due to the effect of changes in market conditions or to subsequent decisions on the activities of the business. These differences may have a material impact on the asset values, impairments and amortisation expense reported in future periods.

Notes to the Financial Statements

for the year ended 31st December 2005

11 Property, plant and equipment

	Leasehold land & buildings 2005 £000	Plant & equipment, fixtures & fittings 2005 £000	Total 2005 £000
Group – 2005			
Cost			
At 1st January 2005	82	13,509	13,591
Additions	–	632	632
Disposals	–	(316)	(316)
At 31st December 2005	82	13,825	13,907
Depreciation			
At 1st January 2005	56	6,001	6,057
Eliminated on disposals	–	(70)	(70)
Charge for the year	12	2,803	2,815
At 31st December 2005	68	8,734	8,802
Net book value			
At 31st December 2005	14	5,091	5,105

	Leasehold land & buildings 2004 £000	Plant & equipment, fixtures & fittings 2004 £000	Total 2004 £000
Group – 2004			
Cost			
At 1st January 2004	82	23,880	23,962
Additions	–	2,823	2,823
On acquisition of businesses and subsidiary undertakings	–	37	37
Disposals	–	(13,231)	(13,231)
At 31st December 2004	82	13,509	13,591
Depreciation			
At 1st January 2004	46	10,948	10,994
Eliminated on disposals	–	(9,573)	(9,573)
Charge for the year	10	4,626	4,636
At 31st December 2004	56	6,001	6,057
Net book value			
At 31st December 2004	26	7,508	7,534

At 31st December 2005, the net book value of assets held under finance leases, capitalised and included in plant and equipment, fixtures and fittings amounts to £nil (2004: £nil). The depreciation charge on such assets during the year amounted to £nil (2004: £10,000).

11 Property, plant and equipment continued

	Plant & equipment, fixtures & fittings 2005 £000
Company – 2005	
Cost	
At 1st January 2005	291
Disposals to other Group companies	(291)
At 31st December 2005	–
Depreciation	
At 1st January 2005	268
Eliminated on disposals to other Group companies	(268)
At 31st December 2005	–
Net book value	
At 31st December 2005	–
	Plant & equipment, fixtures & fittings 2004 £000
Company – 2004	
Cost	
At 1st January 2004	287
Additions	4
At 31st December 2004	291
Depreciation	
At 1st January 2004	229
Charge for the year	39
At 31st December 2004	268
Net book value	
At 31st December 2004	23

12 Capital commitments

	2005 £000	2004 £000
Capital expenditure that has been contracted but not provided for	–	–

Notes to the Financial Statements

for the year ended 31st December 2005

13 Fixed asset investments

	Investment in subsidiaries 2005 £000
Company	
At 1st January 2005	113,698
Capital contributions for share-based payments	425
At 31st December 2005	114,123
	Investment in subsidiaries 2004 £000
Company	
At 1st January 2004	33,298
Impairments	(33,249)
Additions	113,487
Capital contributions for share-based payments	162
At 31st December 2004	113,698

Investments in Group undertakings are stated at cost less impairments. No impairments against cost were taken in the year ended 31st December 2005 (2004: £33,249,000).

Except where stated, the following subsidiary companies are wholly-owned including 100% voting rights, operate in the United Kingdom and are registered in England & Wales. All companies have been included in the consolidated results of the Group.

Principal undertakings

Undertaking	Business
Nestor Primecare Services Limited ¹	UK healthcare services and flexible staffing services in UK health and social care
Care Monitoring 2000 Limited ²	Homecare remote monitoring
Nestor Equipment Leasing Limited ¹	Provision of asset leasing
Helenus Limited	Intermediate holding company

¹ The interest of Nestor Healthcare Group plc is held through intermediate holding companies.

² Nestor Healthcare Group plc has a 51% interest.

The directors consider that to give full particulars of all subsidiary undertakings would lead to a statement of excessive length. A full list of subsidiary undertakings will be annexed to the company's next annual return.

Related party transactions

The Group had no material transactions with related parties during the year. The Company holds amounts due to and due from certain of its subsidiaries at 31st December 2005 (see notes 14 and 16).

Details of any transactions with directors are set out in the Remuneration Report. Compensation of directors and key management is disclosed in note 28.

Business acquisitions

In January 2005, the group purchased one business, Community Careline Services, for a total consideration of £1,800,000, plus capitalised costs of acquisition amounting to £54,000. This purchase has been accounted for as an acquisition. No other acquisitions were made in the year.

In addition, adjustments were made to reduce the total consideration for acquisitions made in 2003 and 2004 by £1,862,000, reflecting the finalisation of contingent consideration payable under the various purchase agreements. Adjustments to goodwill arising on these same acquisitions reflected both the reduction in total consideration and also, for the acquisitions made in 2004, the finalisation of net assets acquired following detailed review.

The provisional fair values of assets and liabilities acquired in the year, which represent their book values, and adjustments thereof relating to the 2003 and 2004 acquisitions, and the goodwill arising are outlined in the table below. All values of assets, liabilities and goodwill arising on the 2005 acquisition will be finalised in the 2006 financial statements when detailed review of the business acquired will be completed.

13 Fixed asset investments continued

	2005 acquisition Community Careline Services £000	Adjustments re 2003 and 2004 acquisitions £000	Total £000
Non-current assets:			
Intangible assets	442	–	442
Current assets and liabilities:			
Trade and other receivables	16	–	16
Trade and other payables	(27)	26	(1)
Net current assets	(11)	26	15
Non-current liabilities:			
Provisions	(80)	(25)	(105)
Net assets acquired	351	1	352
Purchase consideration	1,800	(1,862)	(62)
Costs of acquisition	54	–	54
Total cost	1,854	(1,862)	(8)
Total goodwill arising in year (note 10)	1,503	(1,863)	(360)

	Total £000
Cash flows in respect of purchase of businesses and subsidiary undertakings	
2005 acquisition:	
Total consideration	1,800
Costs of acquisition	54
	1,854
Less: deferred and retained consideration accrued, not yet paid	(150)
	1,704
2003 and 2004 acquisitions:	
Deferred and retained consideration previously accrued, paid in 2005	2,031
Total cash flows in respect of purchase of businesses and subsidiary undertakings	3,735

From the date of acquisition to 31st December 2005, Community Careline Services contributed £2,703,000 to revenue and £424,000 to operating profit.

In the year ended 31st March 2004, the last full financial year prior to acquisition, the branches of Community Careline Services that were subsequently acquired by the Group contributed revenue of £3,695,000, profit before tax of £456,000 and profit after tax of £319,000.

At 31st December 2005 a total of £616,000 of deferred and retained consideration remained to be paid in respect of acquisitions made in 2003, 2004 and 2005 (2004: £4,359,000).

Notes to the Financial Statements

for the year ended 31st December 2005

14 Deferred tax assets

	2005 £000	2004 £000
Group		
Pension liability	4,866	4,602
Accelerated capital allowances	1,833	1,818
Intangible assets	185	82
Share-based payments	176	48
Losses	–	255
Other	276	79
Total potential deferred tax assets	7,336	6,884
Less: losses not relivable	–	(255)
Total recognised deferred tax assets	7,336	6,629

All of the Group deferred tax assets potentially recognisable have been recognised and included in non-current assets. There were no deferred tax assets of the Company at either 31st December 2005 or 31st December 2004.

15 Trade and other receivables

	Group		Company	
	2005 £000	2004 £000	2005 £000	2004 £000
Trade receivables:				
– Gross	32,664	45,546	–	–
– Bad debt provision	(1,914)	(2,496)	–	–
Amounts owed by Group companies	–	–	112,614	126,753
Other debtors	5,618	3,383	–	444
Prepayments and accrued income	3,264	4,495	–	116
Trade and other receivables due within one year	39,632	50,928	112,614	127,313

Concentrations of credit risk with respect to trade receivables are limited due to the Group's customer base being large and unrelated. Accordingly, management believe that there is no further credit risk provision required in excess of normal provision for doubtful receivables.

16 Current liabilities – falling due within one year

	Group		Company	
	2005 £000	2004 £000	2005 £000	2004 £000
Financial liabilities:				
– Bank overdrafts (note 18)	987	1,601	–	7,116
– Bank loans (note 18)	81,000	–	81,000	–
Trade payables	10,120	12,735	–	–
Amounts owed to Group companies	–	–	–	20,200
Deferred consideration for acquisitions	616	4,359	–	–
Other creditors	7,943	6,024	–	777
Accruals and deferred income	3,437	10,969	–	2,521
U.S. payroll tax	1,575	1,577	–	–
Other UK tax and social security	1,956	4,364	–	–
Corporation tax	2,012	2,216	–	–
Provisions (note 20)	2,164	2,112	–	15
Total current liabilities	111,810	45,957	81,000	30,629

17 Non-current liabilities – amounts falling due after more than one year

	Group		Company	
	2005 £000	2004 £000	2005 £000	2004 £000
Financial liabilities:				
– Bank loans (note 18)	–	84,000	–	84,000
Other creditors	–	1	–	–
Provisions (note 20)	17,764	19,728	–	371
Total non-current liabilities	17,764	103,729	–	84,371

18 Net borrowings

	Interest rates	Group		Company	
		2005 £000	2004 £000	2005 £000	2004 £000
Unsecured					
Bank overdraft and loans	variable	(81,987)	(85,601)	(81,000)	(91,116)
Total borrowings		(81,987)	(85,601)	(81,000)	(91,116)
Cash at bank and in hand		2,098	979	–	114
Net borrowings		(79,889)	(84,622)	(81,000)	(91,002)

Net borrowings for the Group are summarised as follows:

	Repayable within 1 year £000	Repayable between 1 & 2 years £000	Total £000
Unsecured:			
Bank overdraft and loans	(81,987)	–	(81,987)
Total borrowings	(81,987)	–	(81,987)
Cash at bank and in hand	2,098	–	2,098
At 31st December 2005	(79,889)	–	(79,889)
At 31st December 2004	(622)	(84,000)	(84,622)

Net borrowings for the Company are summarised as follows

	Repayable within 1 year £000	Repayable between 1 & 2 years £000	Total £000
Unsecured:			
Bank overdraft and loans	(81,000)	–	(81,000)
Total borrowings	(81,000)	–	(81,000)
At 31st December 2005	(81,000)	–	(81,000)
At 31st December 2004	(7,002)	(84,000)	(91,002)

Post-balance sheet event

Since the balance sheet date the Group has renegotiated the renewal of its bank facilities, which had been due to expire in July 2006. A total facility of £90,000,000 has been agreed with a syndicate of three banks to remain in place until December 2009. Borrowing under this facility is secured by a charge created over Group assets. Intercompany borrowing due from one operating subsidiary to the Company has in addition been subordinated to all other borrowings and obligations of that subsidiary.

19 Financial instruments

An explanation of the role that financial instruments have had during the year in creating or changing the risks that the Group faces in its activities is set out in the Financial Review.

Interest rate profile of financial liabilities

The interest rate profile of the Group's financial liabilities at 31st December 2005 was:

	Floating rate financial liabilities £000	Financial liabilities on which no interest paid £000	Total £000
At 31st December 2005 – all sterling	85,694	–	85,694
At 31st December 2004 – all sterling	92,098	1	92,099

All the Group's current liabilities falling due within one year (other than bank and other borrowings and property provisions) are excluded from the above table either due to their short-term nature or because they do not meet the definition of a financial liability, such as tax balances.

Notes to the Financial Statements

for the year ended 31st December 2005

19 Financial instruments continued

All floating rate interest rates are linked to LIBOR. Included in floating rate liabilities are £35,000,000 of borrowings upon which the Group has entered into interest rate swaps that have the effect of restricting LIBOR rates on those borrowings to between 4.0% and 5.6%. The net fair value of these swaps at 31st December 2005 was £nil.

Included in the above are the Group's provisions of £3,707,000 (2004: £6,497,000) for onerous contracts and other property provisions (note 20) which meet the definition of financial liabilities. These financial liabilities are considered to be floating rate liabilities as, in establishing the provisions, the cash flows have been discounted and the discount rate is re-appraised at each half yearly reporting date to ensure that it reflects current market assessments of the time value of money and the risks specific to the liability. Other floating rate financial liabilities bear interest at rates, based on LIBOR, which are fixed in advance for periods of between one month and six months.

Interest rate profile of financial assets

The interest rate profile of the Group's financial assets was:

Currency	Floating rate financial assets 2005 £000	Financial assets on which no interest received 2005 £000	Total 2005 £000
Sterling	1,994	68	2,062
Australian dollars	—	33	33
New Zealand dollars	—	3	3
At 31st December 2005	1,994	104	2,098

Currency	Floating rate financial assets 2004 £000	Financial assets on which no interest received 2004 £000	Total 2004 £000
Sterling	933	22	955
Australian dollars	—	17	17
New Zealand dollars	—	7	7
At 31st December 2004	933	46	979

The financial assets comprise bank deposits, bank current account balances and cash in hand. The floating rate financial assets earn interest at rates based on LIBOR and are all recoverable within one year or on demand. The financial assets on which no interest is received are balances on some bank current accounts and cash in hand.

Maturity of financial liabilities

The maturity profile of the Group's financial liabilities at 31st December 2005 was:

	Borrowings 2005 £000	Property provisions 2005 £000	Other financial liabilities 2005 £000	Total 2005 £000
Within 1 year, or on demand	81,987	1,708	—	83,695
Between 1 and 2 years	—	1,007	—	1,007
Between 2 and 5 years	—	604	—	604
Over 5 years	—	388	—	388
At 31st December 2005	81,987	3,707	—	85,694

	Borrowings 2004 £000	Property provisions 2004 £000	Other financial liabilities 2004 £000	Total 2004 £000
Within 1 year, or on demand	1,601	2,464	1	4,066
Between 1 and 2 years	84,000	1,912	—	85,912
Between 2 and 5 years	—	1,415	—	1,415
Over 5 years	—	706	—	706
At 31st December 2004	85,601	6,497	1	92,099

19 Financial instruments continued

Borrowing facilities

The Group had the following undrawn floating rate committed borrowing facilities available in respect of which all conditions precedent had been met at that date:

	2005 £000	2004 £000
Expiring within 1 year	19,000	–
Expiring between 1 and 2 years	–	16,000
	19,000	16,000

All the above facilities incur commitment fees at market rates.

Fair values of all financial assets and financial liabilities

The following table shows a comparison between the carrying amounts and the fair values of all the Group's financial assets and financial liabilities, including trade and other receivables and trade and other payables, both current and non-current.

Fair value is the amount at which a financial instrument could be exchanged in an arm's length transaction between informed and willing parties, other than a forced or liquidation sale and excludes accrued interest. For floating rate financial assets and liabilities, fair values approximate to book values.

	2005		2004	
	Book value £000	Fair value £000	Book value £000	Fair value £000
Group				
Financial assets – cash at bank and in hand	2,098	2,098	979	979
Short-term financial assets – trade and other receivables	39,632	39,632	50,928	50,928
Short-term financial liabilities – borrowings	(81,987)	(81,987)	(1,601)	(1,601)
Short-term financial liabilities – trade and other payables	(25,647)	(25,647)	(40,028)	(40,028)
Short-term financial liabilities – property provisions	(1,708)	(1,708)	(2,056)	(2,056)
Long-term financial liabilities – borrowings	–	–	(84,000)	(84,000)
Long-term financial liabilities – other payables	–	–	(1)	(1)
Long-term financial liabilities – property provisions	(1,999)	(1,999)	(4,441)	(4,441)
	(69,611)	(69,611)	(80,220)	(80,220)

20 Provisions

	Pensions 2005 £000	Property 2005 £000	Total 2005 £000
Group – 2005			
At 1st January 2005	15,343	6,497	21,840
Contributions paid	(1,719)	–	(1,719)
Current service cost	1,218	–	1,218
Finance charge	325	–	325
Actuarial loss	1,054	–	1,054
Acquired on purchase of businesses	–	105	105
Transfer to profit and loss account	–	(689)	(689)
Utilised in the year	–	(2,435)	(2,435)
Unwinding of discount	–	229	229
At 31st December 2005	16,221	3,707	19,928
Analysed as:			
Provisions estimated to be settled after more than one year	15,765	1,999	17,764
Provisions estimated to be settled within one year	456	1,708	2,164
Total provisions	16,221	3,707	19,928
	Pensions 2005 £000	Property 2005 £000	Total 2005 £000
Company – 2005			
At 1st January 2005	–	386	386
Transfer to other Group companies	–	(386)	(386)
At 31st December 2005	–	–	–

Notes to the Financial Statements

for the year ended 31st December 2005

20 Provisions continued

	Pensions 2004 £000	Property 2004 £000	Total 2004 £000
Group – 2004			
At 1st January 2004	15,671	2,944	18,615
Contributions paid	(2,388)	–	(2,388)
Current service cost	1,500	–	1,500
Finance charge	412	–	412
Actuarial loss	148	–	148
Transfer to profit and loss account	–	3,876	3,876
Utilised in the year	–	(438)	(438)
Unwinding of discount	–	115	115
At 31st December 2004	15,343	6,497	21,840

Analysed as:

Provisions estimated to be settled after more than one year	15,287	4,441	19,728
Provisions estimated to be settled within one year	56	2,056	2,112
Total provisions	15,343	6,497	21,840

	Pensions 2004 £000	Property 2004 £000	Total 2004 £000
Company – 2004			
At 1st January 2004	–	913	913
Transfer to profit and loss account	–	(296)	(296)
Utilised in the year	–	(264)	(264)
Unwinding of discount	–	33	33
At 31st December 2004	–	386	386

Analysed as:

Provisions estimated to be settled after more than one year	–	371	371
Provisions estimated to be settled within one year	–	15	15
Total provisions	–	386	386

Pensions

The actuarial deficits on the Group's two defined benefit pension schemes total £16,221,000 (2004: £15,343,000). The assumptions used in calculating the combined deficit, and description of the schemes and their assets and liabilities generally, are further described in note 30.

Property

The Group has a number of properties that are either vacant or sublet at a discount.

The Group property provision of £3,707,000 comprises £2,182,000 (2004: £4,636,000) in respect of lease contracts for such properties no longer occupied by the Group, £466,000 (2004: £731,000) in respect of associated lease dilapidations, £146,000 (2004: £381,000) in respect of associated other exit costs, and £913,000 (2004: £749,000) in respect of lease dilapidations obligations relating to properties that continue to be occupied.

Provision has been made for onerous lease costs taking into account estimates of the length of time properties will be vacant (net of any potential sub-lease income where this can be estimated with a high degree of probability), together with any dilapidation costs and other costs associated with the termination or disposal of leases. In determining the provision for vacant properties, the cash flows have been discounted using appropriate government bond rates. The estimates used in determining the appropriate level of provision represent management's best view of likely market conditions after taking external advice. Actual activity may differ from these estimates due to the effect of changes in the property market or subsequent business decisions. These differences may have a material impact on the provisions established for these matters.

21 Share capital

	Authorised Number	£000	Allotted, issued and fully paid Number	£000
Ordinary shares of 10p each				
At 1st January 2005	96,000,000	9,600	87,633,070	8,763
At 31st December 2005	96,000,000	9,600	87,633,070	8,763

No shares were issued during the year (2004: 1,645).

22 Share premium account and reserves

	Share premium account 2005 £000	Share payment reserve 2005 £000	Other reserves 2005 £000	Retained (losses)/ earnings 2005 £000
Group – 2005				
At 1st January 2005	43,224	211	864	(21,888)
Share-based payments	–	425	–	–
Actuarial losses arising in defined benefit pension schemes	–	–	–	(1,054)
Deferred taxation arising on actuarial losses	–	–	–	316
Profit for the year	–	–	–	10,251
Dividends	–	–	–	(2,190)
At 31st December 2005	43,224	636	864	(14,565)

At 31st December 2005, goodwill written off in prior years directly against retained earnings/(losses) in respect of subsidiaries still held by the Group was £16,891,000 (31st December 2004 – £16,891,000).

	Share premium account 2005 £000	Share payment reserve 2005 £000	Other reserves 2005 £000	Retained (losses)/ earnings 2005 £000
Company – 2005				
At 1st January 2005	43,224	211	25,750	48,200
Share-based payments	–	425	–	–
Profit for the year	–	–	–	21,354
Dividends	–	–	–	(2,190)
At 31st December 2005	43,224	636	25,750	67,364

Included in other Company reserves at 31st December 2005 and 31st December 2004 are £21,512,000 of distributable reserves and £4,238,000 of non-distributable reserves. The retained earnings of the Company at both dates include £49,307,000 that is not distributable.

	Share premium account 2004 £000	Share payment reserve 2004 £000	Other reserves 2004 £000	Retained (losses)/ earnings 2004 £000
Group – 2004				
At 1st January 2004	43,222	49	864	33,607
Issue of shares	2	–	–	–
Share-based payments	–	162	–	–
Actuarial losses arising in defined benefit pension schemes	–	–	–	(148)
Deferred taxation arising on actuarial losses	–	–	–	44
Loss for the year	–	–	–	(50,010)
Dividends	–	–	–	(5,381)
At 31st December 2004	43,224	211	864	(21,888)

Notes to the Financial Statements

for the year ended 31st December 2005

22 Share premium account and reserves continued

	Share premium account 2004 £000	Share payment reserve 2004 £000	Other reserves 2004 £000	Retained (losses)/ earnings 2004 £000
Company – 2004				
At 1st January 2004	43,222	49	25,750	266,358
Issue of shares	2	–	–	–
Share-based payments	–	162	–	–
Loss for the year	–	–	–	(212,777)
Dividends	–	–	–	(5,381)
At 31st December 2004	43,224	211	25,750	48,200

23 Statement of changes in equity

	2005 £000	2004 £000
Group		
Net recognised income/(expense)	9,716	(49,996)
Shares issued during the year	–	2
Dividends paid	(2,190)	(5,381)
Increase in share payment reserve	425	162
Increase/(decrease) in equity shareholders' funds	7,951	(55,213)
Total equity at beginning of the year	31,224	86,437
Total equity at end of the year	39,175	31,224

	2005 £000	2004 £000
Company		
Net recognised income/(expense)	21,354	(212,777)
Shares issued during the year	–	2
Dividends paid	(2,190)	(5,381)
Increase in share payment reserve	425	162
Increase/(decrease) in total equity	19,589	(217,994)
Total equity at beginning of the year	126,148	344,142
Total equity at end of the year	145,737	126,148

24 Minority interests

	2005 £000	2004 £000
At 1st January	50	(68)
Share of net profit of subsidiaries	203	118
At 31st December	253	50

25 Notes to the cash flow statements

	Group		Company	
	2005	2004	2005	2004
	£000	£000	£000	£000
Reconciliation of profit/(loss) to cash generated from operations				
Profit/(loss) for the year	10,454	(49,892)	21,354	(212,777)
Adjustments for:				
Tax expense/(credit)	3,795	2,364	(1,563)	-
Finance income	(30)	(64)	-	(64)
Finance expense	5,672	5,672	4,959	5,151
Goodwill and investment impairment	-	49,109	-	33,249
Share-based payments	425	162	-	-
Amortisation of intangible assets	344	272	-	-
Depreciation of property, plant and equipment	2,815	4,636	-	39
Profit on sale of property, plant and equipment	(4)	(128)	-	-
Changes in working capital:				
(Decrease)/increase in provisions	(3,187)	3,775	(386)	(527)
Decrease in trade and other receivables	11,312	7,302	16,262	315,832
(Decrease)/increase in creditors	(10,640)	3,484	(23,498)	1,978
Cash generated from operations	20,956	26,692	17,128	142,881

	Group		Company	
	2005	2004	2005	2004
	£000	£000	£000	£000
Reconciliation of net cash flow to movement in net debt				
Increase/(decrease) in cash and cash equivalents	1,119	(1,949)	(114)	(1,204)
Decrease in finance leases	-	14	-	-
Decrease in loans from banks	3,000	6,000	3,000	6,000
(Increase)/decrease in loans other than from banks	-	1,407	-	1,407
Decrease/(increase) in bank overdrafts	614	(750)	7,116	12,721
	4,733	4,722	10,002	18,924
Net debt at beginning of the year	(84,622)	(89,344)	(91,002)	(109,926)
Net debt at end of the year	(79,889)	(84,622)	(81,000)	(91,002)

26 Operating lease commitments

The Group has numerous premises operated under leases whose terms, conditions and expiry dates vary considerably, some of which are no longer occupied by the Group. In addition, the Group leases items of plant and equipment and in particular has entered into a contract hire agreement to lease motor vehicles.

At 31st December 2005 the net commitment in respect of operating leases in 2006 is as follows:

	Plant & equipment including motor vehicles £000	Land & buildings occupied by Group £000	Land & buildings not occupied by Group £000	Total £000
For leases expiring				
within one year	174	667	93	934
between two and five years	327	1,274	354	1,955
beyond five years	-	1,103	703	1,806
	501	3,044	1,150	4,695

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26 Operating lease commitments continued

At 31st December 2004 the net commitment in respect of operating leases in 2005 was as follows:

	Plant & equipment including motor vehicles £000	Land & buildings occupied by Group £000	Land & buildings not occupied by Group £000	Total £000
For leases expiring				
within one year	446	756	420	1,622
between two and five years	216	1,411	–	1,627
beyond five years	–	1,310	1,153	2,463
	662	3,477	1,573	5,712

27 Employees

	2005 £000	2004 £000
Employee costs for the Group		
Wages and salaries	102,305	119,037
Social security costs	7,787	9,213
Pension costs	1,465	1,751
Share-based payments	425	162
	111,982	130,163

	2005	2004
Average number of persons employed		
Full time	1,941	2,381
Part time	5,043	5,800
	6,984	8,181

	2005	2004
Employee numbers by business segment		
Healthcare Staffing	550	831
Social Care	5,015	5,248
Primary Care	1,419	2,102
	6,984	8,181

Employee costs and numbers employed for 2004 have been restated to include all costs and numbers employed for careworkers working within the Social Care business segment, as they are considered to be classed as employees. The employee costs so reclassified for 2004 amount to £66,265,000. The number of careworkers employed so reclassified for 2004 totals 4,519 (293 full time plus 4,226 part time). No such reclassification is appropriate for either the Healthcare Staffing or the Primary Care business segments.

28 Compensation of directors and key management

	2005 £000	2004 £000
Directors and other key management		
Salaries and short-term employee benefits	1,856	2,428
Post-employment benefits	290	356
Termination benefits	–	574
Share-based payments	235	73
	2,381	3,431
	2005 £000	2004 £000
Directors		
Aggregate emoluments	1,020	2,047
Company contributions to money purchase pension schemes	21	52
	1,041	2,099

Aggregate emoluments include £nil (2004: £574,000) compensation for loss of office, including £nil (2004: £75,000) company contributions to money purchase pension schemes.

The detailed numerical analysis of directors' aggregate emoluments is included in the tables in the Remuneration Report on pages 19 to 25 which forms part of these financial statements.

29 Share-based payments

Fair values have been calculated and charged to operating profit for all share-based payments. These consist of grants of shares and share options under various schemes to directors, key managers and other employees. Assumptions used and results of the fair value calculations are set out below.

Assumptions

	Exercise price (pence)	Shares under option at 01.01.04	Shares under option at 01.01.05	Shares under option at 31.12.05	Vesting periods
Savings Related Share Option Scheme – 2003 awards	157.12	818,187	462,442	214,942	3 to 5 years
Savings Related Share Option Scheme – 2004 awards	156.96	–	266,169	157,959	3 to 5 years
Savings Related Share Option Scheme – 2005 awards	121.16	–	–	429,230	3 to 5 years
Share Option Plan 2002 – 2003 awards	273.50 and 301.00	416,748	357,748	243,748	3 years
Share Option Plan 2002 – 2005 awards	152.75 and 114.50	–	–	1,559,057	3 years
Long-term Incentive Plan – deferred shares – 2004 award	–	–	13,076	13,076	3 years
Long-term Incentive Plan – matching shares – 2004 award	–	–	55,405	55,405	3 years
Long-term Incentive Plan – deferred shares – 2005 award	–	–	–	27,923	3 years
Long-term Incentive Plan – matching shares – 2005 award	–	–	–	158,652	3 years
		1,234,935	1,154,840	2,859,992	

The share price used in the calculation of fair value has in each case been the share price on the date of grant.

Notes to the Financial Statements

for the year ended 31st December 2005

29 Share-based payments continued

Savings Related Share Option Scheme awards must be exercised within six months of vesting. Assumed life terms have accordingly been set at either 3.25 years or 5.25 years for these awards. Share Option Plan 2002 awards may be exercised within three to ten years from the date of award. Exercise of these options is assumed to be spread through this period. Fixed three year terms have been assumed for the Long-term Incentive Plan awards.

The expected volatility is based on historical volatility over periods which correspond to the forward life assumptions for each category of award, being 3.25 to 5.25 years for Savings Related Share Option Scheme awards, six years effective average for Share Option Plan 2002 awards and three years for Long-term Incentive Plan awards. Two periods of exceptional volatility have been excluded, with additional historical data substituted in their place.

The risk-free rate of interest assumed is the rate of interest obtainable from government securities over the same expected terms as have been used for the volatility calculations.

The expected dividend yield assumed has been calculated on the basis of publicly available information at the respective grant dates, being the historical dividend yield.

The Long-term Incentive Plan matching shares awards are subject to a total shareholder return ("TSR") vesting condition. This condition has been allowed for in the calculations of fair value.

Lapsing rates of 10% per annum have been assumed for Savings Related Share Option Scheme awards; 7.5% per annum for Share Option Plan 2002 awards and 0% for Long-term Incentive Plan awards.

Results of calculations of fair value

The fair value of share-based transactions has been calculated using a stochastic simulation modelling technique, developed in consultation with an independent third party advisor. The charge so calculated for 2005 is £425,000 (2004: £162,000). The elements of this charge analysed by share-based transaction are as follows:

	Fair value of one option £	Total fair value charge 2005 £000	Total fair value charge 2004 £000
Savings Related Share Option Scheme – 2003 awards	0.55 and 0.54	22	45
Savings Related Share Option Scheme – 2004 awards	0.54	21	23
Savings Related Share Option Scheme – 2005 awards	0.69 and 0.77	51	–
Share Option Plan 2002 – 2003 awards	0.80 and 0.95	68	68
Share Option Plan 2002 – 2005 awards	0.50	204	–
Long-term Incentive Plan – deferred shares – 2004 award	1.81	6	6
Long-term Incentive Plan – matching shares – 2004 award	0.83	15	11
Long-term Incentive Plan – deferred shares – 2005 award	1.44	9	9
Long-term Incentive Plan – matching shares – 2005 award	0.85	29	–
		425	162

30 Pension commitments

The Group has accounted for pensions in accordance with IAS 19 and the disclosures given below are those required by that standard. In accordance with the exemption allowed under IFRS 1, full retrospective application of IAS 19 from the date of commencement of both schemes has not been applied. Accordingly, the differences between liabilities (other than unvested plan changes) and assets have been recognised in full as at 1st January 2004.

Group defined benefit pension schemes

The Group operates two funded pension schemes providing benefits based on final pensionable salary. The two schemes are the Nestor Healthcare Group Retirement Benefits Scheme (the Nestor Scheme) and the Healthcall Group Limited Pension Scheme (the Healthcall Scheme). Both schemes are closed to new members. The schemes are administered by Trustees separately from the affairs of the Group and are contracted out of the additional component of the State Pension Scheme.

Neither scheme holds any investment in any financial instrument issued by the Group. Neither are any of the schemes' property or other assets occupied or used by the Group.

There are no informal practices applied that might give rise to any constructive obligations.

30 Pension commitments continued

Nestor Scheme

Watson Wyatt Limited, consulting actuaries, carried out an actuarial valuation of the Nestor Scheme as at 5th April 2003. On the actuarial basis used, as at that date, the assessed value of the assets was 62% of the value placed on the liabilities in respect of benefits earned to 5th April 2003, allowing for expected future increases in pensionable earnings to Normal Pension Age, treating the scheme as an ongoing entity.

The market value of the investments held in the Nestor Scheme as at the valuation date was £9,923,000. In addition there were pensions in payment secured by the purchase of annuities.

The assumptions which have the most significant effect on the results of the valuation are those relating to the rate of investment return on future net cash flow and the rate of increase in pensionable earnings. These rates were set relative to an assumed long-term rate of price inflation of 2.5% per annum.

The assumed future rate of investment return, used to discount projected income and outgoing benefits, was a real rate of 2.0% per annum relative to price inflation for pensioners and 5.0% per annum before retirement and 3.0% per annum after retirement for non-pensioners. Pensionable earnings were assumed to increase on average at a rate of 2.0% per annum ahead of price inflation with promotional increases assumed in addition.

The employer's contribution rate, currently 22.4% (32.4% for certain current and past executive directors), is calculated using the projected unit method and the shortfall of assets as at 5th April 2003 is amortised as a constant percentage of members' pensionable earnings over the average expected working lifetime of the active members. As the Nestor Scheme is closed to new members, under the projected unit method the employer's contribution rate will increase as the members of that scheme approach retirement.

Healthcall Scheme

Watson Wyatt Limited, consulting actuaries, carried out an actuarial valuation of the Healthcall Scheme as at 1st November 2004. On the actuarial basis used, as at that date, the assessed value of the assets was 62% of the capitalised value of the accrued benefits, allowing for expected future increases in pensionable earnings to Normal Pension Age, treating the scheme as an ongoing entity.

The market value of the investments held in the scheme as at the valuation date was £7,744,000. In addition there were pensions in payment secured by the purchase of annuities.

The assumptions which have the most significant effect on the results of the valuation are those relating to the rate of investment return and the rate of increase in pensionable earnings. These rates were set relative to an assumed long-term rate of price inflation of 2.75% per annum.

The assumed future rate of investment return, used to discount projected income and outgoing benefits, was a real rate of 2.0% per annum relative to price inflation for pensioners and 4.25% per annum before retirement and 2.75% per annum after retirement for non-pensioners. Pensionable earnings were assumed to increase on average at the same rate as price inflation.

The employer's contribution rate, currently 14.9%, is calculated using the projected unit method and the shortfall of assets as at 1st November 2004 is amortised as annual payments of £640,000 over the average remaining expected service lives of the active members. As the Healthcall scheme is closed to new members, under the projected unit method the employer's contribution rate will increase as the members of that scheme approach retirement.

Notes to the Financial Statements

for the year ended 31st December 2005

30 Pension commitments continued

Other schemes

The Group also operates several defined contribution schemes with varying rates of employer contribution.

Pension charge

	2005 £000	2004 £000
Current service cost of defined benefit schemes	1,218	1,500
Group contributions to defined contribution schemes	247	251
	1,465	1,751
Net finance charge relating to defined benefit schemes	325	412
Pension charge	1,790	2,163

At 31st December 2005 £95,000 had yet to be paid to the respective schemes (2004: £121,000).

Valuations

The valuation used for IAS 19 disclosures has been based on the results of an actuarial valuation of the Nestor Scheme as at 5th April 2003 and on the last actuarial valuation of the Healthcall Scheme as at 1st November 2004 and updated by Watson Wyatt Limited to take account of the requirements of IAS 19 in order to assess the liabilities of the schemes at 31st December 2005. Assets of the schemes are stated at their market valuation at 31st December 2005.

The accounting policy applied in respect of recognised actuarial gains and losses is to account for them immediately and in full within the statement of recognised income and expense.

Mortality assumptions

The assumptions relating to longevity underlying the pension liabilities at the balance sheet date are based on standard actuarial mortality tables, and include an allowance for future improvements in longevity. The assumptions are equivalent to expected longevity at age 65 for members in normal health approximately as follows:

- pensioners currently aged 65: males 19 years, females 22 years
- non-pensioners currently aged 45: males 21 years, females 24 years.

Financial assumptions used to calculate the schemes' liabilities

	2005	2004
Valuation method	Projected unit	Projected unit
Discount rate	4.80%	5.40%
Inflation rate	2.80%	2.80%
Increases to pensions in payment and deferred pensions*	2.80%	2.80%
Salary increases	4.75%	4.80%

* Different increases assumed for certain elements of pension

Financial assumptions used to calculate the schemes' net service costs for the year

	2005	2004
Valuation method	Projected unit	Projected unit
Discount rate	5.40%	5.50%
Inflation rate	2.80%	2.80%
Increases to pensions in payment and deferred pensions*	2.80%	2.75%
Salary increases	4.80%	4.75%

* Different increases assumed for certain elements of pension

30 Pension commitments continued

Assets in the schemes and the expected rates of return

	Long-term rate of return expected on 31st December 2005	Value at 31st December 2005 £000	Long-term rate of return expected on 31st December 2004	Value at 31st December 2004 £000
Equities	8.00%	24,452	8.00%	19,252
Bonds	4.25%	2,136	4.75%	1,957
Other	4.00%	3,057	4.00%	2,896
Total market value of assets		29,645		24,105
Present value of schemes' liabilities		(45,866)		(39,448)
Deficit in the schemes – pension liabilities		(16,221)		(15,343)
Related deferred tax asset		4,866		4,602
Net pension liability		(11,355)		(10,741)

The expected return for each asset class reflects a combination of historical performance analysis, the forward looking views of the financial markets (as suggested by the yields available) and the views of investment organisations. Consideration is also given to the rate of return expected to be available for reinvestment. The overall expected rate of return on assets is derived as the weighted average of the expected returns from each of the main asset classes.

Movement in the deficit in the schemes during the year

	2005 £000	2004 £000
Deficit in the schemes at beginning of the year	(15,343)	(15,671)
Contributions paid	1,719	2,388
Current service cost	(1,218)	(1,500)
Other finance charge	(325)	(412)
Actuarial loss	(1,054)	(148)
Deficit in the schemes at end of the year	(16,221)	(15,343)

Components of defined benefit cost for the year

	2005 £000	2004 £000
Analysis of amounts charged to operating profit		
Current service cost	1,218	1,500
Analysis of amounts charged to finance expense		
Interest on pension scheme liabilities	2,138	1,969
Expected return on assets in the pension scheme	(1,813)	(1,557)
Net charge to finance expense	325	412
Total income statement charge before deduction for tax	1,543	1,912

Analysis of amounts recognised in the statement of recognised income and expense

	2005 £000	2004 £000
Actual return on assets	5,065	1,985
Expected return on assets	(1,813)	(1,557)
Actuarial gain on assets	3,252	428
Experience losses arising on the scheme liabilities	(4,306)	(576)
Actuarial loss recognised in the statement of recognised income and expense	(1,054)	(148)

Notes to the Financial Statements

for the year ended 31st December 2005

30 Pension commitments continued

Reconciliation of the present value of defined benefit obligation ("DBO")

	2005 £000	2004 £000
Present value of DBO at start of the year	39,448	36,163
Service cost	1,218	1,500
Interest cost	2,138	1,969
Employee contributions	219	338
Actuarial loss	4,306	576
Actual benefit payments including expenses	(1,463)	(1,098)
Present value of DBO at end of the year	45,866	39,448

Reconciliation of the fair value of assets

	2005 £000	2004 £000
Present value of assets at start of the year	24,105	20,492
Expected return on assets	1,813	1,557
Actuarial gain	3,252	428
Group contributions	1,719	2,388
Employee contributions	219	338
Actual benefit payments	(1,157)	(685)
Administration expenses paid	(306)	(413)
Fair value of assets at end of the year	29,645	24,105

History of experience adjustments

	2005 £000	2004 £000
Present value of defined benefit obligations	(45,866)	(39,448)
Fair value of scheme assets	29,645	24,105
Deficit in the schemes at the end of the year	(16,221)	(15,343)

	2005	2004
Experience gains/(losses) on scheme liabilities:		
Amount (£'000)	(4,306)	(576)
Percentage of present value of scheme liabilities	(9.4%)	(1.5%)
Experience gains/(losses) on scheme assets:		
Amount (£'000)	3,252	428
Percentage of present value of scheme assets	11.0%	1.8%

31 Share option schemes

The following table sets out options in issue under the various Company schemes at the beginning and end of the year and movements during the year. Share options in issue expire after a certain time and exercise dates vary. Exercise rights are subject to the rules of the schemes and share options in issue are not normally exercisable until the expiry of a period of at least three years. In addition, achievement of performance targets is normally required in all schemes except the Savings Related Share Option ("SAYE") Scheme.

	Date of issue	Option price (pence)	In issue 1st Jan 2005	Granted in the year	Exercised in the year	Lapsed in the year	In issue 31st Dec 2005
Company Share Option Plan 1996							
	April 1998	236.50	4,661	–	–	–	4,661
	October 1998	339.50	4,602	–	–	–	4,602
	April 1999	407.50	17,541	–	–	(9,543)	7,998
	October 1999	596.50	26,875	–	–	(13,960)	12,915
	May 2000	425.00	159,296	–	–	(73,420)	85,876
	August 2000	429.50	6,984	–	–	(6,984)	–
	November 2000	472.50	6,349	–	–	(6,349)	–
	March 2001	542.50	33,724	–	–	(9,198)	24,526
	October 2001	510.00	35,292	–	–	(17,646)	17,646
	April 2002	544.00	11,028	–	–	–	11,028
			306,352	–	–	(137,100)	169,252
Employee Share Option Scheme 1996							
	April 1998	236.50	63,687	–	–	(15,221)	48,466
	April 1999	407.50	31,603	–	–	(11,186)	20,417
	October 1999	596.50	2,850	–	–	(2,850)	–
	May 2000	425.00	267,306	–	–	(160,837)	106,469
	August 2000	429.50	6,985	–	–	(6,985)	–
	November 2000	472.50	46,561	–	–	(46,561)	–
	March 2001	542.50	159,148	–	–	(93,142)	66,006
	October 2001	510.00	70,882	–	–	(21,568)	49,314
	April 2002	544.00	39,522	–	–	–	39,522
			688,544	–	–	(358,350)	330,194
Share Option Plan 2002							
	July 2002	267.50	567,214	–	–	(365,910)	201,304
	October 2002	212.50	322,352	–	–	(150,588)	171,764
	June 2003	273.50	112,248	–	–	–	112,248
	November 2003	301.00	245,500	–	–	(114,000)	131,500
	January 2005	152.75	–	1,467,354	–	–	1,467,354
	November 2005	114.50	–	91,703	–	–	91,703
			1,247,314	1,559,057	–	(630,498)	2,175,873
Savings Related Share Option Scheme							
	September 1999	412.00	5,565	–	–	(5,565)	–
	April 2001	447.20	14,103	–	–	(3,997)	10,106
	April 2002	454.80	43,471	–	–	(32,943)	10,528
	April 2003	157.12	462,442	–	–	(247,500)	214,942
	April 2004	156.96	266,169	–	–	(108,210)	157,959
	April 2005	121.16	–	515,121	–	(85,891)	429,230
			791,750	515,121	–	(484,106)	822,765
Total			3,033,960	2,074,178	–	(1,610,054)	3,498,084

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32 Reconciliation of net assets and profit under UK GAAP to IFRS

The Group reported under UK GAAP in its previously published financial statements for the year ended 31st December 2004. The analysis below provides a reconciliation of net assets and profit as reported under UK GAAP as at 31st December 2004 to the revised net assets and profit under IFRS as reported in these financial statements. In addition, a reconciliation is provided of net assets under UK GAAP to IFRS at the transition date for the Group, being 1st January 2004.

Reconciliation of the Group profit and loss account under UK GAAP to the Group income statement under IFRS for the year ended 31st December 2004

	UK GAAP		Total £000
	Before goodwill amortisation and exceptional items £000	Goodwill amortisation and exceptional items £000	
Revenue	389,839	–	389,839
Cost of sales	(291,361)	–	(291,361)
Gross profit	98,478	–	98,478
Administrative expenses	(77,835)	(8,841)	(86,676)
Operating profit/(loss) before fundamental restructuring cost	20,643	(8,841)	11,802
Exceptional loss on disposal of subsidiary undertaking	–	(1,577)	(1,577)
Goodwill impairment	–	(48,613)	(48,613)
Other fundamental restructuring costs	–	(11,831)	(11,831)
Operating (loss)/profit	20,643	(70,862)	(50,219)
Finance income	–	–	–
Finance expense	(5,418)	–	(5,418)
(Loss)/profit before taxation	15,225	(70,862)	(55,637)
Tax expense	(4,605)	2,170	(2,435)
(Loss)/profit for the year	10,620	(68,692)	(58,072)
Profit attributable to minority interests	118	–	118
Loss/(profit) attributable to equity shareholders	10,502	(68,692)	(58,190)
(Loss)/profit for the year	10,620	(68,692)	(58,072)
(Loss)/earnings per 10p share			
Basic	11.98p	(78.38p)	(66.40p)
Diluted	11.98p	(78.38p)	(66.40p)
Equity dividends	1,314	–	1,314
Dividends per share	1.50p	–	1.50p

IFRS reclassifications			IFRS remeasurements					IFRS
Goodwill impairment £000	Exceptional items £000	Other items £000	Goodwill amortisation IFRS 3 £000	Amortisation of intangible assets IFRS 3 £000	Share-based payments charge IFRS 2 £000	Employee benefits IAS 19 £000	Timing of dividend charge recognition IAS 10 £000	£000
-	-	-	-	-	-	-	-	389,839
-	-	-	-	-	-	-	-	(291,361)
-	-	-	-	-	-	-	-	98,478
(48,613)	(13,408)	-	8,345	(272)	(162)	388	-	(140,398)
(48,613)	(13,408)	-	8,345	(272)	(162)	388	-	(41,920)
-	1,577	-	-	-	-	-	-	-
48,613	-	-	-	-	-	-	-	-
-	11,831	-	-	-	-	-	-	-
-	-	-	8,345	(272)	(162)	388	-	(41,920)
-	-	64	-	-	-	-	-	64
-	-	(64)	-	-	-	(190)	-	(5,672)
-	-	-	8,345	(272)	(162)	198	-	(47,528)
-	-	-	-	82	48	(59)	-	(2,364)
-	-	-	8,345	(190)	(114)	139	-	(49,892)
-	-	-	-	-	-	-	-	118
-	-	-	8,345	(190)	(114)	139	-	(50,010)
-	-	-	8,345	(190)	(114)	139	-	(49,892)
-	-	-	9.52p	(0.21p)	(0.13p)	0.15p	-	(57.07p)
-	-	-	9.52p	(0.21p)	(0.13p)	0.15p	-	(57.07p)
-	-	-	-	-	-	-	4,067	5,381
-	-	-	-	-	-	-	4.64p	6.14p

Notes to the Financial Statements

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32 Reconciliation of net assets and profit under UK GAAP to IFRS continued

Reconciliation of the Group balance sheet under UK GAAP to IFRS as at 31st December 2004

	UK GAAP £000	IFRS reclass- ifications £000	IFRS remeasurements					IFRS £000
			Goodwill amortisation IFRS 3 £000	Amortisation of intangible assets IFRS 3 £000	Share-based payments charge IFRS 2 £000	Employee benefits IAS 19 £000	Timing of dividend charge recognition IAS 10 £000	
			£000	£000	£000	£000	£000	
Non-current assets								
Goodwill	106,767	(913)	8,345	-	-	-	-	114,199
Other intangible assets	-	913	-	(272)	-	-	-	641
Property, plant and equipment	7,534	-	-	-	-	-	-	7,534
Deferred tax assets	-	3,144	-	82	48	3,355	-	6,629
Non-current assets	114,301	3,144	8,345	(190)	48	3,355	-	129,003
Current assets								
Trade and other receivables	50,928	-	-	-	-	-	-	50,928
Deferred tax assets	3,144	(3,144)	-	-	-	-	-	-
Cash and cash equivalents	979	-	-	-	-	-	-	979
Current assets	55,051	(3,144)	-	-	-	-	-	51,907
Current liabilities								
Financial liabilities:								
Borrowings – overdrafts	(1,601)	-	-	-	-	-	-	(1,601)
Trade and other payables	(41,342)	-	-	-	-	-	1,314	(40,028)
Current tax liabilities	(2,216)	-	-	-	-	-	-	(2,216)
Provisions	-	(2,348)	-	-	-	236	-	(2,112)
Current liabilities	(45,159)	(2,348)	-	-	-	236	1,314	(45,957)
Net current assets	9,892	(5,492)	-	-	-	236	1,314	5,950
Total assets less current liabilities	124,193	(2,348)	8,345	(190)	48	3,591	1,314	134,953
Non-current liabilities								
Financial liabilities:								
Borrowings – loans	(84,000)	-	-	-	-	-	-	(84,000)
Other payables	(1)	-	-	-	-	-	-	(1)
Provisions	(10,655)	2,348	-	-	-	(11,421)	-	(19,728)
Non-current liabilities	(94,656)	2,348	-	-	-	(11,421)	-	(103,729)
Net assets	29,537	-	8,345	(190)	48	(7,830)	1,314	31,224
Equity								
Called up share capital	8,763	-	-	-	-	-	-	8,763
Share premium account	43,224	-	-	-	-	-	-	43,224
Share payment reserve	-	-	-	-	211	-	-	211
Other reserves	864	-	-	-	-	-	-	864
Retained losses	(23,364)	-	8,345	(190)	(163)	(7,830)	1,314	(21,888)
Equity shareholders' funds	29,487	-	8,345	(190)	48	(7,830)	1,314	31,174
Equity minority interests	50	-	-	-	-	-	-	50
Total equity	29,537	-	8,345	(190)	48	(7,830)	1,314	31,224

32 Reconciliation of net assets and profit under UK GAAP to IFRS continued

Reconciliation of the Group balance sheet under UK GAAP to IFRS as at 1st January 2004 (date of transition to IFRS)

	UK GAAP	IFRS reclassifications	IFRS remeasurements					IFRS
			Goodwill amortisation IFRS 3	Amortisation of intangible assets IFRS 3	Share-based payments charge IFRS 2	Employee benefits IAS 19	Timing of dividend charge recognition IAS 10	
	£000	£000	£000	£000	£000	£000	£000	£000
Non-current assets								
Goodwill	161,085	–	–	–	–	–	–	161,085
Property, plant and equipment	12,968	–	–	–	–	–	–	12,968
Deferred tax assets	–	3,228	–	–	–	3,370	–	6,598
Non-current assets	174,053	3,228	–	–	–	3,370	–	180,651
Current assets								
Trade and other receivables	58,268	–	–	–	–	–	–	58,268
Deferred tax assets	3,228	(3,228)	–	–	–	–	–	–
Cash and cash equivalents	2,928	–	–	–	–	–	–	2,928
Current assets	64,424	(3,228)	–	–	–	–	–	61,196
Current liabilities								
Financial liabilities:								
Borrowings – overdrafts	(851)	–	–	–	–	–	–	(851)
Borrowings – loans	(1,421)	–	–	–	–	–	–	(1,421)
Trade and other payables	(46,405)	–	–	–	–	–	5,381	(41,024)
Current tax liabilities	(3,495)	–	–	–	–	–	–	(3,495)
Provisions	–	(953)	–	–	–	(198)	–	(1,151)
Current liabilities	(52,172)	(953)	–	–	–	(198)	5,381	(47,942)
Net current assets	12,252	(4,181)	–	–	–	(198)	5,381	13,254
Total assets less current liabilities	186,305	(953)	–	–	–	3,172	5,381	193,905
Non-current liabilities								
Financial liabilities:								
Borrowings – loans	(90,000)	–	–	–	–	–	–	(90,000)
Other payables	(4)	–	–	–	–	–	–	(4)
Provisions	(7,380)	953	–	–	–	(11,037)	–	(17,464)
Non-current liabilities	(97,384)	953	–	–	–	(11,037)	–	(107,468)
Net assets	88,921	–	–	–	–	(7,865)	5,381	86,437
Equity								
Called up share capital	8,763	–	–	–	–	–	–	8,763
Share premium account	43,222	–	–	–	–	–	–	43,222
Share payment reserve	–	–	–	–	49	–	–	49
Other reserves	864	–	–	–	–	–	–	864
Retained earnings	36,140	–	–	–	(49)	(7,865)	5,381	33,607
Equity shareholders' funds	88,989	–	–	–	–	(7,865)	5,381	86,505
Equity minority interests	(68)	–	–	–	–	–	–	(68)
Total equity	88,921	–	–	–	–	(7,865)	5,381	86,437

Notes to the Financial Statements

for the year ended 31st December 2005

32 Reconciliation of net assets and profit under UK GAAP to IFRS continued

Reconciliation of the Company balance sheet under UK GAAP to IFRS as at 31st December 2004

	UK GAAP	IFRS reclass- ifications	IFRS remeasurements					IFRS
			Goodwill amortisation IFRS 3	Amortisation of intangible assets IFRS 3	Share-based payments charge IFRS 2	Employee benefits IAS 19	Timing of dividend charge recognition IAS 10	
	£000	£000	£000	£000	£000	£000	£000	£000
Non-current assets								
Investments	113,487	~	-	-	211	-	-	113,698
Property, plant and equipment	23	~	-	-	-	-	-	23
Non-current assets	113,510	~	-	-	211	-	-	113,721
Current assets								
Trade and other receivables	560	~	-	-	-	-	-	560
Amounts owed by Group companies	151,753	~	-	-	-	-	(25,000)	126,753
Cash and cash equivalents	114	~	-	-	-	-	-	114
Current assets	152,427	~	-	-	-	-	(25,000)	127,427
Current liabilities								
Financial liabilities:								
Borrowings – overdrafts	(7,116)	~	-	-	-	-	-	(7,116)
Amounts owed to Group companies	(20,200)	~	-	-	-	-	-	(20,200)
Dividends proposed	(1,314)	~	-	-	-	-	1,314	-
Trade and other payables	(3,298)	~	-	-	-	-	-	(3,298)
Provisions	-	(15)	-	-	-	-	-	(15)
Current liabilities	(31,928)	(15)	-	-	-	-	1,314	(30,629)
Net current assets	120,499	(15)	-	-	-	-	(23,686)	96,798
Total assets less current liabilities	234,009	(15)	-	-	211	-	(23,686)	210,519
Non-current liabilities								
Financial liabilities:								
Borrowings – loans	(84,000)	~	-	-	-	-	-	(84,000)
Provisions	(386)	15	-	-	-	-	-	(371)
Non-current liabilities	(84,386)	15	-	-	-	-	-	(84,371)
Net assets	149,623	-	-	-	211	-	(23,686)	126,148
Equity								
Called up share capital	8,763	~	-	-	-	-	-	8,763
Share premium account	43,224	~	-	-	-	-	-	43,224
Share payment reserve	-	~	-	-	211	-	-	211
Other reserves	25,750	~	-	-	-	-	-	25,750
Retained earnings	71,886	~	-	-	-	-	(23,686)	48,200
Equity shareholders' funds	149,623	-	-	-	211	-	(23,686)	126,148
Equity minority interests	-	~	-	-	-	-	-	-
Total equity	149,623	-	-	-	211	-	(23,686)	126,148

32 Reconciliation of net assets and profit under UK GAAP to IFRS continued

Reconciliation of the Company balance sheet under UK GAAP to IFRS as at 1st January 2004 (date of transition to IFRS)

	UK GAAP £000	IFRS reclass- ifications £000	IFRS remeasurements					IFRS £000
			Goodwill amortisation IFRS 3 £000	Amortisation of intangible assets IFRS 3 £000	Share-based payments charge IFRS 2 £000	Employee benefits IAS 19 £000	Timing of dividend charge recognition IAS 10 £000	
Non-current assets								
Investments	33,249	–	–	–	49	–	–	33,298
Property, plant and equipment	58	–	–	–	–	–	–	58
Deferred tax assets	–	5	–	–	–	–	–	5
Non-current assets	33,307	5	–	–	49	–	–	33,361
Current assets								
Trade and other receivables	811	–	–	–	–	–	–	811
Amounts owed by Group companies	464,329	–	–	–	–	–	(22,000)	442,329
Deferred tax assets	5	(5)	–	–	–	–	–	–
Cash and cash equivalents	1,318	–	–	–	–	–	–	1,318
Current assets	466,463	(5)	–	–	–	–	(22,000)	444,458
Current liabilities								
Financial liabilities:								
Borrowings – overdrafts	(19,837)	–	–	–	–	–	–	(19,837)
Borrowings – loans	(1,407)	–	–	–	–	–	–	(1,407)
Amounts owed to Group companies	(19,876)	–	–	–	–	–	–	(19,876)
Dividends proposed	(5,381)	–	–	–	–	–	5,381	–
Trade and other payables	(1,644)	–	–	–	–	–	–	(1,644)
Provisions	–	(15)	–	–	–	–	–	(15)
Current liabilities	(48,145)	(15)	–	–	–	–	5,381	(42,779)
Net current assets	418,318	(20)	–	–	–	–	(16,619)	401,679
Total assets less current liabilities	451,625	(15)	–	–	49	–	(16,619)	435,040
Non-current liabilities								
Financial liabilities:								
Borrowings – loans	(90,000)	–	–	–	–	–	–	(90,000)
Provisions	(913)	15	–	–	–	–	–	(898)
Non-current liabilities	(90,913)	15	–	–	–	–	–	(90,898)
Net assets	360,712	–	–	–	49	–	(16,619)	344,142
Equity								
Called up share capital	8,763	–	–	–	–	–	–	8,763
Share premium account	43,222	–	–	–	–	–	–	43,222
Share payment reserve	–	–	–	–	49	–	–	49
Other reserves	25,750	–	–	–	–	–	–	25,750
Retained earnings	282,977	–	–	–	–	–	(16,619)	266,358
Equity shareholders' funds	360,712	–	–	–	49	–	(16,619)	344,142
Equity minority interests	–	–	–	–	–	–	–	–
Total equity	360,712	–	–	–	49	–	(16,619)	344,142

Notes to the Financial Statements

for the year ended 31st December 2005

33 Reconciliations from UK GAAP to IFRS: explanatory notes

Notes to IFRS reclassifications

Notes to income statement reclassifications

Certain income statement items, previously reported under UK GAAP, have been reclassified to comply with the format of the Group's accounts as presented under IFRS. The reclassifications below do not have any effect on the Group's previously reported profit/(loss).

(i) Goodwill impairment

Goodwill impairment associated with the reduction of the carrying value of the Healthcall group of companies acquired in 2001 was accounted for within exceptional items under UK GAAP in 2004. The amount so impaired in the year to 31st December 2004 was £48,613,000. Under IFRS this has been charged to operating profit and reclassified accordingly out of exceptional items. £496,000 previously accounted for within goodwill amortisation and impairment in the year to 31st December 2004 has in addition been reclassified as goodwill impairment and charged to operating profit.

(ii) Exceptional items

The total of exceptional items charged under UK GAAP was £62,021,000 in the year to 31st December 2004. Of this amount, £48,613,000 related to goodwill impairment; this charge has been reclassified as a charge to operating profit as described in (i) above. The other exceptional items charged, amounting to £13,408,000 in the year to 31st December 2004, have been reclassified under IFRS so that they have instead also been charged to operating profit.

The impact of items (i) and (ii) together is that all amounts previously charged to exceptional items under UK GAAP, being either goodwill impairment or other exceptional items, have been charged to operating profit under IFRS.

(iii) Finance income and expense

Under UK GAAP the net of interest payable and receivable, described as net interest payable, was shown as one figure in the profit and loss account. Under IFRS the requirement is to show interest payable and receivable separately in the income statement, and to be renamed finance expense and finance income respectively.

Notes to balance sheet reclassifications

(i) IFRS 3 – Business combinations (identification of intangible assets)

IFRS 3 requires that wherever possible fair values are ascribed to identified intangible assets acquired via business combinations, as a result of which the amounts ascribed to pure goodwill arising on consolidation would be correspondingly reduced. An exercise has therefore been carried out to identify all such intangible assets acquired through the Group's purchases of all companies and businesses since 1st January 2004. Assets so identified amount to £913,000 as at 31st December 2004, chiefly representing the net present value of discounted future cash flows deriving from customer contracts. This value has been transferred from goodwill to other intangible assets.

(ii) Deferred taxation

As required by IFRS, values of deferred tax assets are always classed as receivables due after more than one year, disclosed within non-current assets.

(iii) Provisions

As required by IFRS, values of provisions have been separately analysed between current liabilities due within one year and non-current liabilities due after more than one year. The former amounts have accordingly been disclosed separately on the balance sheet within current liabilities, whilst the latter amounts have been disclosed separately within non-current liabilities.

Notes to IFRS remeasurements

Remeasurements under IFRS have been applied as follows:

(i) IFRS 3 – Business combinations (goodwill amortisation)

Under UK GAAP, goodwill is required to be amortised over its estimated useful economic life. On transition to IFRS, the balance of goodwill recognised under UK GAAP at that date is "frozen" and no further amortisation is charged. The effect is that goodwill amortisation that had been charged, amounting to £8,345,000 in the year to 31st December 2004, has under IFRS been added back in arriving at operating profit.

(ii) IFRS 3 – Business combinations (identification of intangible assets)

IFRS 3 requires that wherever possible fair values are ascribed to identified intangible assets acquired via business combinations, as a result of which the amounts ascribed to pure goodwill arising on consolidation would be correspondingly reduced. An exercise has therefore been carried out to identify all such intangible assets acquired through the Group's purchases of all companies and businesses since 1st January 2004. Assets so identified amount to £913,000 as at 31st December 2004, chiefly representing the net present value of discounted future cash flows deriving from customer contracts. IFRS requires that this value is amortised over the respective contract lives. The amount so charged is £272,000 in the year to 31st December 2004.

33 Reconciliations from UK GAAP to IFRS: explanatory notes continued

(iii) IFRS 2 – Share-based payments

The Group's employee share and share option schemes, including long-term incentive plans and other awards potentially available to directors, have been accounted for in accordance with IFRS 2. This requires that a charge be recognised for all of these schemes. Previously under UK GAAP no such charges had been taken. The amount so charged under IFRS is £162,000 in the year to 31st December 2004. A credit corresponding to this amount has at the same time been made to a newly created share payment reserve within equity shareholders' funds.

The charges made under IFRS have been calculated using fair values derived from use of a stochastic simulation modelling technique.

(iv) IAS 19 – Employee benefits

Pensions have been accounted for under IAS 19. The Group's accounting policy is to recognise immediately any actuarial gains and losses relating to its defined benefit pension schemes in full in the statement of recognised income and expense. Accordingly, the pension scheme deficits are included as liabilities in the balance sheet. The additional liability so recognised is £11,235,000 as at 1st January 2004 and £11,185,000 as at 31st December 2004. Deferred tax assets relating to these additional liabilities have been recognised within non-current assets, amounting to £3,370,000 as at 1st January 2004 and £3,355,000 as at 31st December 2004.

These amounts (both gross deficits and associated deferred tax assets) recognised under IFRS are additional to the recognition of the actuarial deficit on the Healthcall pension scheme under UK GAAP following the acquisition of the Healthcall group of companies in 2001.

The impact on profit/(loss) before taxation arising from the adoption of IAS 19 in the year to 31st December 2004 is an increase of £198,000, representing a reduction of £388,000 in operating costs, partially offset by an increase of £190,000 in finance expense.

(v) IAS 10 – Events after the balance sheet date (dividends)

IAS 10 requires that dividends in respect of the Group's ordinary shares not declared until after the balance sheet date are only noted, but not accrued in the balance sheet. Previously, under UK GAAP, such dividends were accounted for in the presentation of retained earnings, and accrued in the balance sheet. The impact is that the final dividend of £5,381,000 (6.14p per share) payable in respect of 2003, which was declared only in May 2004, has under IFRS been accounted for in 2004 rather than in 2003.

The final dividend for 2004 of £1,314,000 (1.50p per share) was accounted for in that year under UK GAAP. Under IFRS this dividend is accounted for in 2005, when declared.

Five Year Summary

	2001 £000	2002 £000	2003 £000	2004 £000	2005 £000
Group income statement					
Revenue	400,965	482,695	423,161	389,839	309,035
Operating profit/(loss)	21,629	29,669	20,392	(41,920)	19,891
Exceptional items	(4,574)	(17,300)	(2,680)	–	–
Profit/(loss) before net finance expense	17,055	12,369	17,712	(41,920)	19,891
Net finance expense	(1,544)	(4,238)	(4,110)	(5,608)	(5,642)
Profit/(loss) before taxation	15,511	8,131	13,602	(47,528)	14,249
Tax expense	(6,013)	(6,052)	(4,353)	(2,364)	(3,795)
Profit/(loss) for the year	9,498	2,079	9,249	(49,892)	10,454
Profit/(loss) attributable to shareholders	9,479	2,031	9,202	(50,010)	10,251
Profit attributable to equity minority interests	19	48	47	118	203
Profit/(loss) for the year	9,498	2,079	9,249	(49,892)	10,454
Basic earnings/(loss) per 10p share	11.55p	2.33p	10.51p	(57.07p)	11.70p

The results for 2004 and 2005 are presented consistent with the application of IFRS. The results for prior years are presented consistent with UK GAAP as had then been applied. Results for these years are not therefore directly comparable with those for 2004 and 2005.

In particular, material differences are as follows:

Items that would have been charged to exceptional items under UK GAAP were charged to operating profit under IFRS in 2004;

Goodwill amortisation that was charged under UK GAAP in 2003 and prior years was not charged under IFRS in 2004 or 2005;

Intangible assets have been recognised and amortised under IFRS in 2004 and 2005;

A charge for share-based payments has been made under IFRS in 2004 and 2005;

Charges relating to defined benefit pension schemes have been calculated differently under IFRS than had been the case under UK GAAP.

It should be noted that the 2004 operating loss is stated after charging £62,021,000 that had been accounted for as exceptional items, including goodwill impairment, under UK GAAP.

2002 has been restated to reflect the full adoption of FRS 19. 2001 has not been restated as it is not practicable to determine the impact of FRS 19 with sufficient accuracy.

	2001 £000	2002 £000	2003 £000	2004 £000	2005 £000
Group balance sheet					
Goodwill	152,507	138,049	161,085	114,199	113,839
Other intangible assets	–	–	–	641	739
Property, plant and equipment	13,512	12,741	12,968	7,534	5,105
Other non-current assets	28	1	–	6,629	7,336
Total non-current assets	166,047	150,791	174,053	129,003	127,019
Current assets excluding cash	66,024	59,187	61,496	50,928	39,632
Current and non-current liabilities excluding borrowings	(63,131)	(61,898)	(57,284)	(64,085)	(47,587)
Net operating assets	168,940	148,080	178,265	115,846	119,064
Net borrowings	(75,350)	(59,761)	(89,344)	(84,622)	(79,889)
Net assets	93,590	88,319	88,921	31,224	39,175
Share capital	8,708	8,747	8,763	8,763	8,763
Share premium account	42,298	43,022	43,222	43,224	43,224
Other reserves	42,271	36,229	37,004	(20,813)	(13,065)
Equity shareholders' funds	93,277	87,998	88,989	31,174	38,922
Equity minority interests	313	321	(68)	50	253
Total equity	93,590	88,319	88,921	31,224	39,175
Group cash flow statement					
Net cash inflow from operating activities before exceptional items	24,648	54,144	24,990	26,692	20,956
Cash flow from exceptional items	(2,246)	(2,300)	(1,899)	–	–
Interest paid	(964)	(3,896)	(3,744)	(5,556)	(5,526)
Tax paid	(6,268)	(6,240)	(5,711)	(3,930)	(4,390)
Capital expenditure, net	(4,523)	(6,743)	(5,730)	(2,543)	(382)
Acquisitions and disposals	(124,934)	(12,640)	(29,285)	(4,562)	(3,735)
Equity dividends paid	(5,883)	(7,499)	(8,420)	(5,381)	(2,190)
Issue of shares	38,285	763	216	2	–
Decrease/(increase) in loans and overdrafts	69,679	(10,404)	25,229	(6,671)	(3,614)
Increase/(decrease) in cash	(12,206)	5,185	(4,354)	(1,949)	1,119

The figures for 2004 and 2005 are presented consistent with the application of IFRS. The figures for prior years are presented consistent with UK GAAP as had then been applied. Figures for these years are not therefore directly comparable with those for 2004 and 2005.

In particular, material differences are as follows:

Items that would have been charged to exceptional items under UK GAAP were charged to operating profit under IFRS in 2004;
Goodwill amortisation that was charged under UK GAAP in 2003 and prior years was not charged under IFRS in 2004 or 2005;
Intangible assets have been recognised and amortised under IFRS in 2004 and 2005;
Deficits relating to defined benefit pension schemes have been incorporated into balance sheets under IFRS.

2002 has been restated to reflect the full adoption of FRS 19. 2001 has not been restated as it is not practicable to determine the impact of FRS 19 with sufficient accuracy.

Shareholder Information

Financial calendar

Announcement of 2006 results (provisional)

For the half-year	August 2006
For the year	March 2007
Annual Report and Accounts circulated	March 2007
Annual General Meeting	April 2007

Dividends

Proposed final dividend 2005	
Announcement	9th March 2006
Ex-dividend	3rd May 2006
Record date	5th May 2006
Payment date	2nd June 2006

Interim dividend 2006 (provisional)	
Announcement	August 2006
Payment	October 2006

Analysis of shareholdings

At the date of this report the Company has 1,236 shareholders who hold 87,633,070 ordinary shares between them, analysed as follows:

Size of holding	Number of shareholders	% of shareholders	Number of shares	% of shares
1 – 5,000	960	77.67	1,020,650	1.16
5,001 – 50,000	169	13.67	2,599,008	2.97
50,001 – 100,000	31	2.51	2,331,583	2.66
100,001 and over	76	6.15	81,681,829	93.21
	1,236	100.00	87,633,070	100.00

Type of shareholder

Individuals	832	67.31	1,805,873	2.06
Nominee companies*	361	29.21	85,596,083	97.68
Other corporate and public bodies	43	3.48	231,114	0.26
	1,236	100.00	87,633,070	100.00

* This category includes the beneficiaries of pension funds, unit trusts, life assurance companies and investment trusts.

Share registrar

The Company's registrar is Computershare Investor Services PLC, PO Box 82, The Pavilions, Bridgwater Road, Bristol BS99 7NH.

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